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Fleshing Out the Skeleton: Defining the Prongs of *Stern v. Marshall*

*Robert Miller**

I. INTRODUCTION

Does the action stem from the bankruptcy itself? Is the action necessarily resolved by the claims allowance process? Following *Stern v. Marshall*,[1] these two prongs form the disjunctive test for the constitutional authority of bankruptcy judges to enter final judgments. However, beyond the explicit answers provided by *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*[2] and *Stern* (the Constitutional Adjudication Case Line), the boundaries of these two inquires remain uncertain more than a year after *Stern* was decided. One issue that *Stern* made clear is that state-law-based[3] tort and contract claims cannot be finally adjudicated if they are not completely adjudicated in the process of ruling on the creditor's proof of claim.[4]

The preeminent issue surrounding *Stern* is whether its holding should be applied to only state-law-based counterclaims existing outside of the Bankruptcy Code (the Code)[5] or whether it should be

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1. 131 S. Ct. 2594 (2011).

2. *See* 458 U.S. 50, 90 (1982) (Rehnquist, J., concurring).

3. Courts often use loose wording by employing state law to signify "all nonbankruptcy law that creates substantive claims." Grogan v. Garner, 498 U.S. 279, 284 n.9 (1991) (using the term's "expansive" definition of state law). Even *Stern* and *Marathon* alternate between the terms "state-law-based" and "common-law-based" actions. The correct term would probably be best defined negatively—as an action that does not stem from the bankruptcy itself. In positive terms, this would encompass actions based on state law, actions based on federal nonbankruptcy law, and bankruptcy actions that can be reclassified as common-law actions.

4. *Stern*, 131 S. Ct. at 2615 ("Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, without consent of the litigants, and subject only to ordinary appellate review . . . . Substitute 'tort' for 'contract,' and that statement directly covers this case." (citations omitted)).

5. 11 U.S.C.A. §§ 101-1532 (West 2012).

applied more broadly.[6] As analyzed by many courts, including the Ninth Circuit and Professor Brubaker, it appears *Stern* imported the case line analyzing the Seventh Amendment right to a jury trial[7] (the Seventh Amendment Case Line) into the analysis of the constitutional boundaries of Article I bankruptcy power.[8] This Article assumes that the Constitutional Adjudication Case Line embraces the Seventh Amendment Case Line as precedent for the Article III right to adjudicate inquiry. In attempting to define the boundaries of the two prongs of the *Stern* test, this Article uses post-*Stern* opinions whenever possible. When necessary, it resorts to using the Seventh Amendment Case Line and other cases construing the right to a jury trial to help define the prongs of the *Stern* test.

This Article does not wholly subscribe to Brubaker's other conclusion that the Constitutional Adjudication Case Line reconstitutionalized the summary/plenary dichotomy. In at least three examples—(1) the liquidation of nondischargeable debts, (2) § 502 claims allowance, and (3) turnover—this argument is particularly vulnerable. The summary/plenary dichotomy possesses the force of tradition, "if for no other reason than it went without constitutional challenge for so long under the [Bankruptcy Act of 1898]" (the 1898 Act).[9] The traditional argument[10] rings particularly hollow for late additions to the 1898 Act

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6. *Compare* Black, Davis, & Shue Agency, Inc. v. Frontier Ins. Co. in Rehab. (*In re* Black, Davis, & Shue Agency, Inc.), 471 B.R. 381, 400–01 (Bankr. M.D. Pa. 2012) (suggesting that the narrow view applies *Stern* to core claims under § 157 and the broad view applies it to any "claims that arise outside the Bankruptcy Code"), *with* Menotte v. United States (*In re* Custom Contractors, LLC), 462 B.R. 901, 907–08 (Bankr. S.D. Fla. 2011) (suggesting that the narrow view of *Stern* applies its test only to state-law-based counterclaims while the broad view applies it to other actions including fraudulent conveyances). This Article does not characterize *Stern's* holding by comparing the narrow view against the broad view. As with many things regarding *Stern*, the characterization of the scope of its holding is messy.

7. Langenkamp v. Culp, 498 U.S. 42 (1990) (per curiam); Granfinanciera, S.A. v. Nordberg, 492 U.S. 33 (1989); Katchen v. Landy, 382 U.S. 323 (1966); Schoenthal v. Irving Trust Co., 287 U.S. 92 (1932).

8. *E.g.*, Exec. Benefits Ins. Agency v. Arkison (*In re* Bellingham Ins. Agency, Inc.), 702 F.3d 553, 563 (9th Cir. 2012); Weisfelner v. Blavatnik (*In re* Lyondell Chem. Co.), 467 B.R. 712, 721–22 (S.D.N.Y. 2012) (asserting that *Stern* incorporates the Seventh Amendment Case Line); *see also* Ralph Brubaker, *A "Summary" Statutory and Constitutional Theory of Bankruptcy Judges' Core Jurisdiction after* Stern v. Marshall, 86 AM. BANKR. L.J. 121, 155 (2012) [hereinafter Brubaker, *Statutory and Constitutional Theory*]. *Compare* Moyer v. Koloseik (*In re* Sutton), 470 B.R. 462, 468–69 (Bankr. W.D. Mich. 2012) (suggesting courts apply the Chief Justice's analysis to other parts of 28 U.S.C. § 157(b)), *with* Tanguy v. West (*In re* Davis), No. 07-33986-H3-7, 2012 WL 2871662, at *2 (S.D. Tex. July 10, 2012) (finding that *Stern* does not apply as precedent to the jury trial issue).

9. Meoli v. Huntington Nat'l Bank (*In re* Teleservices Grp.), 456 B.R. 318, 325 (Bankr. W.D. Mich. 2011).

10. The power of tradition itself, as a reason for constitutionality, is questionable. *Compare* Shaffer v. Heitner, 433 U.S. 186, 211–12 (1977) (noting that tradition itself is not sufficient to

such as the discharge amendments enacted in 1970 (the Discharge Amendments), less than ten years before the Bankruptcy Reform Act of 1978 (the Reform Act) that ended the application of the summary/plenary dichotomy. The boundaries of the claims allowance process have always been set by statute and expanded or contracted at the will of the sovereign. The limits of the claims allowance process used pursuant to the 1898 Act do not hamper Congress's power to alter them today. Moreover, *Stern* explicitly found the claims allowance process to be part of the Article I bankruptcy power. Lastly, the test for turnover employed by the 1898 Act does not implicate the Article III concerns of the Constitutional Adjudication Case Line. A different test should be applied to decide whether a bankruptcy court can constitutionally adjudicate a turnover action. In summary, the better view is that "[t]he historical understanding of the plenary/summary distinction informs, but does not dictate" whether a bankruptcy court can constitutionally adjudicate an action.[11]

This Article has five parts. First, it provides a historical overview of both bankruptcy courts' constitutional power to enter final judgments (Constitutional Power) and the relevant impact of the Seventh Amendment on that power. Many prior works have analyzed the facts of *Stern*, the Seventh Amendment Case Line, and the Supreme Court cases analyzing the public rights exception.[12] Hence, this part focuses on cases and sources hitherto overlooked, or at least underanalyzed. In the next two parts, this Article considers the meaning of the two prongs of *Stern*: (1) necessarily resolved by the claims allowance process and (2) stems from the bankruptcy itself. It does not provide a handy list of every conceivable application of these inquiries in bankruptcy.[13] Instead, it considers some of the techniques used to invoke or deflect *Stern* and their application to different causes of ac-

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sustain jurisdiction), *with* Burnham v. Superior Court of Cal., 495 U.S. 604, 619 (1990) (noting that tradition is vital, if not sufficient, to sustain jurisdiction).

11. West v. Freedom Med., Inc. (*In re* Apex Long Term Acute Care–Katy, L.P.), 465 B.R. 452, 462 (Bankr. S.D. Tex. 2011).

12. *E.g.*, Alan M. Ahart, *A Stern Reminder that the Bankruptcy Court Is Not a Court of Equity*, 86 AM. BANKR. L.J. 191, 192 (2012); Douglas G. Baird, *Blue Collar Constitutional Law*, 86 AM. BANKR. L.J. 3, 4–5 (2012) (discussing the public rights exception in light of *Stern*); Christopher S. Lockman, *Makalidung's Post: How* Stern v. Marshall *Is Shaking Bankruptcy Court Jurisdiction to Its Core*, 50 DUQ. L. REV. 125, 152–54 (2012); Jolene Tanner, Comment, Stern v. Marshall*: The Earthquake that Hit the Bankruptcy Courts and the Aftershocks that Followed*, 45 LOY. L.A. L. REV. 587, 590–93 (2012).

13. The possibilities are endless, as *Stern* "has become the mantra of every litigant who, for strategic or tactical reasons, would rather litigate somewhere other than the bankruptcy court." *In re* Ambac Fin. Grp., 457 B.R. 299, 308 (Bankr. S.D.N.Y. 2011). For an excellent summary of the application of *Stern*, see Tyson A. Crist, Stern v. Marshall*: Application of the Supreme Court's Landmark Decision in the Lower Courts*, 86 AM. BANKR. L.J. 627 (2012).

tion by analyzing both post-*Stern* precedent and, when necessary, pre-*Stern* Seventh Amendment cases. In the last part, it considers nondischargeability suits and the constitutionality of bankruptcy courts' power to liquidate a nondischargeable debt. Applying the lessons of *Katchen* and *Stern*, courts should employ the dischargeability allowance process when there are no assets in the estate. Similar to the claims allowance process, if all factual and legal issues presented by liquidating a nondischargeable debt will be decided by the bankruptcy court's judgment on dischargeability, the bankruptcy court may constitutionally adjudicate the liquidation of the nondischargeable debt.

II. CONSTITUTIONAL JURISDICTION OF BANKRUPTCY COURTS: FINAL JUDGMENTS

This Part provides an overview of the Constitutional Power of bankruptcy courts by proceeding chronologically in four stages. First, it will consider the English bankruptcy regime at the time of the ratification of the United States Constitution in 1789 through the Bankruptcy Act of 1867 (the 1867 Act). Next, it will outline the 1898 Act, the first permanent federal bankruptcy statute. It subsequently analyzes the Reform Act and the Code, as well as the changes wrought by *Marathon*. Lastly, it will consider the enactment of the Bankruptcy Amendments and Federal Judgeship Act of 1984 (BAFJA) and *Stern*.

A. *The Common Law, the Founding, and the Early Acts*

Article I of the Constitution empowers Congress to establish uniform federal bankruptcy laws and federal bankruptcy courts.[14] On the one hand, Congress may use its federal bankruptcy power to create Article I bankruptcy courts staffed by bankruptcy judges who are not required to receive the same benefits of life tenure and salary protection bestowed on Article III judges.[15] On the other hand, Congress's bankruptcy power is not boundless because an Article III judge must preside over "the stuff of the traditional actions at common law tried by the courts at Westminster in 1789."[16] The independence provided by the retention and pay protection of Article III is an important buttress against either the legislative or the executive branch's attempt to

14. Congress has the power "[t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States" and "[t]o constitute Tribunals inferior to the supreme [sic] Court." U.S. CONST. art. I, § 8, cl. 4, 9.

15. *See* Stern v. Marshall, 131 S. Ct. 2594, 2609 (2011).

16. N. Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 90 (1982) (Rehnquist, J., concurring).

disrupt the separation of powers.[17] When questions of adjudication arise over whether an Article I bankruptcy judge or an Article III district judge is sufficient, Article III supervision is presumed to be necessary.[18]

Even though "[b]ankruptcy jurisdiction, as understood today and at the time of the framing, is principally *in rem* jurisdiction . . . [t]he Framers would have understood that laws on the subject of Bankruptcies included laws providing, in certain limited respects, for more than simple adjudications of rights in the res."[19] Deciphering how far the Constitutional Power of bankruptcy courts extends beyond "simple adjudications of rights in the res" has proven to be a difficult task.[20]

The importance of the unsatisfactory English system of bankruptcy used in 1789[21] stems from the requirement of the Constitutional Adjudication Case Line that an Article III court adjudicate actions that were "the stuff of the traditional actions at common law tried by the courts at Westminster in 1789."[22] The significance of this archaic framework is magnified by the technique of looking beneath a cause of action to potentially reclassify it as outside the realm of bankruptcy court final adjudication. This technique will be considered in Part V(B). In 1789, English bankruptcy jurisdiction concerned the property of the bankrupt; succinctly summarized, it was in rem.[23] The bankruptcy commissioners, appointed by the Lord Chancellor, "took the bankrupt's property, assigned it, and distributed the proceeds to

17. *Id.* at 57–60, 60 n.10.

18. *Stern*, 131 S. Ct. at 2618 (citing *Marathon Pipe Line Co.*, 458 U.S. at 70 n.23).

19. Cent. Va. Cmty. Coll. v. Katz, 546 U.S. 356, 369–70 (2006) (citations omitted) (internal quotation marks omitted).

20. *Cf. id.* at 370, 372 ("Whatever the appropriate appellation, those who crafted the Bankruptcy Clause would have understood it to give Congress the power to authorize courts to avoid preferential transfers and to recover the transferred property.").

21. Contemporaneous sources described the system as slow, expensive, nonuniform, and corrupt. John C. McCoid, II, *Right to Jury Trial in Bankruptcy:* Granfinanciera, S.A. v. Nordberg, 65 AM. BANKR. L.J. 15, 31 (1991).

22. *Stern*, 131 S. Ct. at 2609 (quoting *Marathon Pipe Line Co.*, 458 U.S. at 90 (Rehnquist, J., concurring)). In his concurrence in *Stern*, Justice Scalia also sought to limit Article I adjudicatory power to "firmly established historical practice." *Id.* at 2621 (Scalia, J., concurring); *see also* Kent L. Richland, Stern v. Marshall*: A Dead-End Marathon?*, 28 EMORY BANKR. DEV. J. 393, 415 (2012). Whether such a category would include actions that could be summarily adjudicated under the 1898 Act or instead would revert to the notions of bankruptcy jurisdiction employed at the time of the founding is unclear; however, considering Justice Scalia's citation of Professor Plank's article that analyzes English bankruptcy practice at the time of the founding and American bankruptcy practice under the 1800 Act, it would appear that those would be relevant areas of inquiry. *See Stern*, 131 S. Ct. at 2621 (Scalia, J., concurring) (citing Thomas E. Plank, *Why Bankruptcy Judges Need Not and Should Not Be Article III Judges*, 72 AM. BANKR. L.J. 567, 607–09 (1998)).

23. Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 123.

the creditors who had proved their claims."[24] The commissioner's jurisdiction did not extend to deciding what constituted the bankruptcy estate.[25] Counterclaims by the estate and avoidance of preferences and fraudulent transfers were among the proceedings outside of the commissioner's jurisdiction.[26] The adjudication of what constituted the bankruptcy estate required actions by the assignees in the courts of law and equity.[27] The early American bankruptcy statutes employed this bifurcation of bankruptcy jurisdiction.[28]

Unfortunately, little information can be gleaned from eighteenth and nineteenth century practices as federal bankruptcy laws rarely existed. Although Congress enacted federal regimes following financial disasters in 1800, 1841, and 1867, in each instance, it quickly repealed the legislation.[29] The Bankruptcy Act of 1800 (the 1800 Act) was cribbed from the then-contemporary English bankruptcy statute.[30] Bankruptcy commissioners, who were not Article III judges, adjudicated proceedings under the 1800 Act.[31] Decisions by the commissioners were subject to review by Article III district court judges.[32] Just like the earlier English procedure, the assignees to the debtor's property, counterparts to contemporary trustees, prosecuted actions against third parties in courts of law and equity.[33] Sadly for originalists, the Supreme Court's reliance on a case decided under the Bankruptcy Act of 1841 (the 1841 Act) as authority for the 1800 Act's interpretation illustrates the paucity of authority interpreting the 1800 Act.[34] The 1841 Act vested jurisdiction over bankruptcy proceedings with the district court. The proceedings were "in the nature of summary proceedings in equity."[35] The 1867 Act implemented a system

24. McCoid, *supra* note 21, at 29.

25. *Id.* at 30.

26. *See* Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 123–24 (citing Halford v. Gillow, 60 Eng. Rep. 18, 20 (Ch. 1842)); McCoid, *supra* note 21, at 30.

27. Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 123; McCoid, *supra* note 21, at 30–31; *see* Meoli v. Huntington Nat'l Bank (*In re* Teleservices Grp.), 456 B.R. 318, 327 (Bankr. W.D. Mich. 2011). However, the commissioner made the initial determination that the actions were property of the debtor. Plank, *supra* note 22, at 613.

28. *See* McCoid, *supra* note 21, at 33–36.

29. Cent. Va. Cmty. Coll. v. Katz, 546 U.S. 356, 386 (2006) (Thomas, J., dissenting) (citing Charles Jordan Tabb, *The History of the Bankruptcy Laws in the United States*, 3 AM. BANKR. INST. L. REV. 5, 13–14 (1995) [hereinafter Tabb, *History*]). See Jonathan C. Lipson, *Debt and Democracy: Towards a Constitutional Theory of Bankruptcy*, 83 NOTRE DAME L. REV. 605, 631–32 (2008), for an interesting commentary on why enactments were so "spasmodic."

30. Lipson, *supra* note 29, at 633.

31. Plank, *supra* note 22, at 608.

32. *Id.* at 609.

33. *Id.* at 613.

34. *Katz*, 546 U.S. at 374 (citing *In re* Comstock, 6 F. Cas. 237, 239 (Vt. 1842)).

35. Tabb, *History*, *supra* note 29, at 17 (internal quotation marks omitted).

of adjudication similar to that later employed under the 1898 Act and the Code. Although the district courts had original jurisdiction over bankruptcy proceedings, they were empowered to appoint registers to assist the district judges.[36] These registers were the forerunners to the later referees and bankruptcy judges.[37] The 1867 Act authorized registers to take control of the debtor's property, adjudicate claims against the property, and then distribute it.[38] However, the registers could not adjudicate any factual or legal objections,[39] and the exact boundaries of their Constitutional Power were uncertain.[40]

B. *The 1898 Act*

The 1898 Act was the first permanent national bankruptcy law,[41] and it clarified the Constitutional Power of the newly created bankruptcy referees.[42] Under the 1898 Act, the bankruptcy referees[43] exercised summary jurisdiction over the assets of the debtor's estate while the now defunct circuit courts, as well as the district courts, exercised plenary jurisdiction over adverse parties to the estate.[44] Summary jurisdiction included adjudication of all claims against the estate.[45] Plenary jurisdiction arose over trustees' suits to recover

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36. *Id.* at 19.

37. *Id.*

38. Melodie Freeman-Burney, *Jurisdiction Under the Bankruptcy Amendments of 1984: Summing Up the Factors*, 22 TULSA L.J. 167, 170 n.23 (1986); *see also In re* Bank of N.C., 2 F. Cas. 668, 669 (E.D.N.C. 1879).

39. Freeman-Burney, *supra* note 38, at 170 n.23; *see also In re Bank of N.C.*, 2 F. Cas. at 669.

40. *See In re Bank of N.C.*, 2 F. Cas. at 669.

41. Cent. Va. Cmty. Coll. v. Katz, 546 U.S. 356, 386 (2006) (Thomas, J., dissenting). Similar to the previous statutes, it was enacted in response to financial panics in 1884 and 1893. Tabb, *History*, *supra* note 29, at 23. By vesting adjudicative power with the district courts, the 1841 Act evaded the morass of issues presented by Article I adjudication. *See id.* at 17.

42. See Ralph Brubaker, *On the Nature of Federal Bankruptcy Jurisdiction: A General Statutory and Constitutional Theory*, 41 WM. & MARY L. REV. 743, 764–67 (2000) [hereinafter Brubaker, *Federal Bankruptcy Jurisdiction*], for an in-depth consideration of the motivation for this change. As a result of this tightening, "[t]he primary vice of the 1898 Act's jurisdictional regime was that it engendered an excessive amount of preliminary litigation over jurisdictional issues surrounding the bifurcation of bankruptcy jurisdiction." *Id.* at 792. Following *Stern*, we face the same vice. George W. Kuney, Stern v. Marshall*: A Likely Return to the Bankruptcy Act's Summary/Plenary Distinction in Article III Terms*, 21 J. BANKR. L. & PRAC. 1 (2012) (suggesting a congressional fix is necessary to forestall "[d]ecades of [l]itigation").

43. This title originated from the process used by district courts to send or refer cases to the bankruptcy courts. Leslie R. Masterson, *Waiving the Right to a Jury: Claims, Counterclaims, and Informal Claims*, 85 AM. BANKR. L.J. 91, 97 (2011). Ironically, the registers of the 1867 Act were also referred cases by the district court. *E.g.*, *In re Bank of N.C.*, 2 F. Cas. at 669.

44. *E.g.*, *In re* Freeway Foods of Greensboro, Inc., 466 B.R. 750, 762 (Bankr. M.D.N.C. 2012).

45. Thus, the bankruptcy referee's jurisdiction was basically in rem. N. Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 97 (1982) (White, J., dissenting).

property or money from third parties who had not filed a claim.[46] Summary proceedings were adjudicated without a jury trial while the right to a jury trial attached to plenary proceedings.[47] Summary jurisdiction encompassed three types of matters: (1) "administrative matters," (2) "matters where the court had actual or constructive possession of a res," and (3) "matters where the parties consented."[48]

Consent proved the most thorny and ambiguous of the three types, and it has remained troublesome.[49] Express and implied consent remain important ways to obtain jurisdiction, even when jurisdiction would not otherwise be proper.[50] In *Stern*, for instance, Pierce Marshall consented to the bankruptcy court's adjudication of his defamation claim by his failure to object and his comments illustrating his contentment with litigating his claim in bankruptcy court, even though the bankruptcy court may not have had statutory jurisdiction over such an action.[51] Under the 1898 Act, express consent of a litigant could waive the right to a plenary proceeding and allow a referee to

46. Ralph Brubaker, *Article III's Bleak House (Part I): The Statutory Limits of Bankruptcy Judges' Core Jurisdiction*, 31 No. 8 BANKR. L. LETTER 1, 7 (2011) [hereinafter Brubaker, *Article III's Bleak House*]; *see* Schoenthal v. Irving Trust Co., 287 U.S. 92, 94–95 (1932). This description overstates the clarity between summary and plenary. For example, the division between a trustee holding a colorable claim to property that can then be adjudicated summarily and a stranger to the estate holding a substantial right to property claim by the estate that must be plenarily adjudicated is blurry. *Compare* May v. Henderson, 268 U.S. 111, 115 (1925) (noting that the trustee's colorable claim to property held by a stranger to the estate allowed a summary proceeding), *with* Harrison v. Chamberlin, 271 U.S. 191, 194–95 (1926) (noting that the trustee must resort to a plenary proceeding when a stranger possessed a substantial right to the property claimed by the estate).

47. Brubaker, *Article III's Bleak House*, *supra* note 46, at 10.

48. Ronald R. Peterson, Stern v. Marshall *Bleak House Revisited,* 27 NABT-TALK 10, 12 (2011).

49. *Compare* Hagan v. Classic Prods. Corp. (*In re* Wilderness Crossings, LLC), No. 09-14547, 2011 WL 5417098, at *4 (Bankr. W.D. Mich. Nov. 8, 2011) (finding that a defaulting defendant consented to bankruptcy court adjudication of a claim, which the court noted was questionable under *Stern*), *with* Moyer v. Koloseik (*In re* Sutton), 470 B.R. 462, 474–76 (Bankr. W.D. Mich. 2012) (disagreeing with *In re Wilderness Crossings* and finding that a defaulting defendant had not consented to bankruptcy court adjudication of a turnover action that the court found the bankruptcy court could not adjudicate pursuant to *Stern*).

50. Stern v. Marshall, 131 S. Ct. 2594, 2607–08 (2011). Whether consent of the litigants is sufficient to allow Article I adjudication of an action that otherwise requires Article III adjudication is questionable. *See* Commodity Futures Trading Comm'n v. Schor, 478 U.S. 833, 851 (1986); Richland, *supra* note 22, at 415. However, bankruptcy courts have found consent sufficient to allow bankruptcy court final adjudication of a core but precluded claim. *See, e.g.*, Penson Fin. Servs., Inc. v. O'Connell (*In re* Arbco Capital Mgmt., LLP), 479 B.R. 254, 262 (S.D.N.Y. 2012) (listing cases); Dev. Specialists, Inc. v. Akin Gump Strauss Hauer & Feld LLP, 462 B.R. 457, 466–67 (S.D.N.Y. 2012).

51. *Stern*, 131 S. Ct. at 2606–08, 2607 n.4.

make a summary adjudication.[52] Following *Stern*, a split between two courts of appeals has arisen over the ability of a litigant to consent to a bankruptcy court's final adjudication of an action that a bankruptcy court could not otherwise finally decide.[53] The Sixth Circuit explained that the right to an Article III adjudication is both a personal right of the litigant and a structural principle of protecting the separation of power between the three branches of government.[54] Because "the encroachment or aggrandizement of one branch at the expense of the other"[55] is implicated by *Stern*, the court found that the structural principle predominates, and a litigant cannot waive the structural principle of Article III adjudication.[56] In contrast, the vast majority of other courts, including the Ninth Circuit, has determined that the personal right of the litigant predominates over the structural principle.[57] The Ninth Circuit explained that "the allocation of authority between bankruptcy courts and district courts does not implicate structural interests, because bankruptcy judges are officer[s] of the district court and are appointed by the Courts of Appeals."[58]

During the 1898 Act, implied consent derived from "a voluntary assertion of a claim by an adverse claimant" against estate property and it "had a peculiarly erratic history."[59] Early cases found that creditors who filed a proof of claim had not implicitly consented to bankruptcy court adjudication of counterclaims for affirmative relief by a

52. MacDonald v. Plymouth Cnty. Trust Co., 286 U.S. 263, 267 (1932); *Consent to Summary Jurisdiction*, 34 FORDHAM L. REV. 469, 471 (1966), *available at* http://ir.lawnet.fordham.edu/flr/vol34/iss3/7.

53. *Compare* Waldman v. Stone, 698 F.3d 910, 918 (6th Cir. 2012), *with* Exec. Benefits Ins. Agency v. Arkison (*In re* Bellingham Ins. Agency, Inc.), 702 F.3d 553, 567 (9th Cir. 2012).

54. *Waldman*, 698 F.3d at 918.

55. *Id.* (quoting *Schor*, 478 U.S. at 850) (internal quotation marks omitted).

56. *Id.* The results of an inability to consent are concerning. Not only will it further increase the workload of Article III courts, but also it could "give litigants a basis to challenge, by reconsideration or appeal, the finality, and therefore the enforceability, of bankruptcy court decisions." Crist, *supra* note 13, at 650.

57. *In re Bellingham Ins. Agency, Inc.*, 702 F.3d at 567 n.9; *see also* Men's Sportswear, Inc. v. Sasson Jeans, Inc. (*In re* Men's Sportswear, Inc.), 834 F.2d 1134, 1138 (2d Cir. 1987); Exec. Sounding Bd. Assocs. Inc. v. Advanced Mach. & Eng'g Co. (*In re* Oldco M Corp.), No. 09-13412 (MG), 2012 WL 6625324, at *5–6 (Bankr. S.D.N.Y. Dec. 20, 2012).

58. *In re Bellingham Ins. Agency, Inc.*, 702 F.3d at 567 n.9 (quoting 28 U.S.C.A. § 151 (West 2012)) (internal quotation marks omitted). This area has already been the subject of significant learned scholarship and is outside the central scope of this Article. *See* Ralph Brubaker, *The Constitutionality of Litigant Consent to Non-Article III Bankruptcy Adjudication*, 32 NO. 12 BANKR. LAW LETTER 1, 5–14 (2012) [hereinafter Brubaker, *Litigant Consent*]; Erwin Chemerinsky, *Formalism Without a Foundation:* Stern v. Marshall (Nov. 27, 2011), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1965604.

59. *Consent to Summary Jurisdiction*, *supra* note 52, at 471.

trustee.[60] This trend changed when the Supreme Court in *Alexander v. Hillman* allowed an equity receivership to obtain summary jurisdiction over counterclaims against creditors.[61] Analogizing bankruptcy trustees to receivers,[62] courts in the mid-twentieth century found that the filing of a proof of claim constituted implied consent to summary jurisdiction of compulsory and even permissive counterclaims by the trustee.[63] However, *Katchen* shifted the focus of the analysis from the consent of the creditor to the bankruptcy court's duty to adjudicate claims.[64] The touchstone became the degree of overlap between the trustee's claim and the adjudication of the creditor's proof of claim.[65]

Although the Supreme Court has embraced implied consent as a basis for Article I adjudication by the Commodity Futures Trading Commission (CFTC), the filing of a proof of claim does not constitute consent to bankruptcy court adjudication. In *Commodity Futures Trading Commission v. Schor*, the Supreme Court embraced a version of implied consent similar to that employed before *Katchen* to allow adjudication of a common-law counterclaim by the CFTC.[66] However, the defendant to the counterclaim in *Schor* was the original plaintiff and had possessed the option to pursue a case in federal dis-

60. *Id.* at 473. A subcategory of cases limited jurisdiction by the amount of a counterclaim compared to the proof of claim. Note, *In the Matter of Counterclaims in Bankruptcy: Summary Procedure and the Jurisdiction of the Bankruptcy Referee*, 65 YALE L.J. 694, 696 n.11 (1956). As long as the counterclaim did not outstrip the creditor's claim it could be summarily adjudicated in bankruptcy court. *Id.* at 694–95.

61. 296 U.S. 222, 238 (1935).

62. "[S]everal courts seized upon *Hillman* to extend the summary jurisdiction of bankruptcy courts." William J. Rochelle, Jr. & John L. King, *Summary Jurisdiction in Bankruptcy:* Katchen v. Landy *and Questions Left Unanswered*, 1966 DUKE L.J. 669, 676, *available at* http://scholarship.law.duke.edu/dlj/vol15/iss3/2.

63. Courts initially distinguished between compulsory and permissive counterclaims. *See, e.g., In re* Solar Mfg. Corp., 200 F.2d 327, 333 (3d Cir. 1952). Most bankruptcy courts were unwilling to summarily adjudicate a permissive counterclaim. *See, e.g., id.* at 333. Prior to *Katchen v. Landy*, 382 U.S. 323 (1966), only the Tenth Circuit expressly allowed summary jurisdiction over permissive counterclaims. *Consent to Summary Jurisdiction*, *supra* note 52, at 479 (citing Inter-State Nat'l Bank v. Luther, 221 F.2d 382 (10th Cir. 1955), *cert. granted*, 350 U.S. 810, *cert. dismissed*, 350 U.S. 944 (1956)). *But see* Stern v. Marshall, 131 S. Ct. 2594, 2617 (2011) (noting that even a debtor's compulsory counterclaim does not automatically create constitutional jurisdiction).

64. *See Katchen*, 382 U.S. at 332 n.9; *Consent to Summary Jurisdiction*, *supra* note 52, at 479–80 (expressing surprise that *Katchen* did not rely on implied consent arising from filing a proof of claim); Rochelle & King, *supra* note 62, at 680 (noting that *Katchen* failed to rely on the consent theory).

65. *See Katchen*, 382 U.S. at 333–34 (explaining that if a bankruptcy court must decide a counterclaim against a creditor who has filed a proof of claim as part of allowing the creditor's claim, then findings would be res judicata for the purposes of later plenary proceedings brought by the debtor on the basis of the counterclaim); *see also* Schwartz v. Levine & Malin, Inc. (*In re* Kelner), 111 F.2d 81, 82 (2d Cir. 1940) (per curiam).

66. *See* Commodity Futures Trading Comm'n v. Schor, 478 U.S. 833, 850–57 (1986).

trict court.[67] In bankruptcy, once the § 362(a) automatic stay arises, an unsecured creditor faces a Hobson's choice of either participating in the bankruptcy by filing a proof of claim or receiving nothing from the distribution of the debtor's estate.[68] Because a creditor filing a proof of claim in bankruptcy cannot choose to pursue the debt elsewhere, both *Granfinanciera* and *Stern* rejected that filing a proof claim constituted implied consent to bankruptcy court adjudication of an estate's counterclaim.[69]

C. *The Reform Act,* Marathon, *and the BAFJA*

In 1978, the Reform Act enacted the Code and restructured bankruptcy jurisdiction to eliminate the distinction between summary and plenary proceedings.[70] The renamed bankruptcy judges[71] were vested with all the "powers of . . . equity, law, and admiralty."[72] Hence, bankruptcy courts had jurisdiction over "all civil proceedings arising under . . . or arising in or related to cases under [the Code]."[73] Although the Reform Act granted bankruptcy judges with jurisdiction similar to Article III judges, it bestowed neither the title of Article III judges nor their salary protection and life tenure.[74]

Marathon found that the bankruptcy courts' enlarged Constitutional Power under the Reform Act violated Article III by granting too much adjudicatory power to an Article I court.[75] Although they disagreed on the scope of the public rights exception, both the plurality and Justice Rehnquist's concurrence found that a state-law-based

67. *But see Stern*, 131 S. Ct. at 2614 ("Pierce did not truly consent to resolution of Vickie's claim in the bankruptcy court proceedings. He had nowhere else to go if he wished to recover from Vickie's estate.").

68. *Id.* at 2615 n.8 (explaining how creditors "have no choice but to file their claims in bankruptcy proceedings if they want to pursue the claims at all"); Masterson, *supra* note 43, at 91 (explaining the interesting origins of Hobson's choice and how a creditor "must either refrain from filing proofs of claims, thereby preserving their jury rights but foregoing any distribution from the estate, or file proofs of claim, thereby retaining their rights against the estate but losing their entitlement to a jury." (quoting *In re* Hooker Invs., Inc., 122 B.R. 659, 663 (S.D.N.Y. 1991)) (internal quotation marks omitted)).

69. *Stern*, 131 S. Ct. at 2614; Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 59 n.14 (1989).

70. N. Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 54 (1982).

71. They were actually renamed earlier as part of the Bankruptcy Rules promulgated on October 1, 1973. *See* Peter F. Coogan, *The Proposed Bankruptcy Act of 1973: Questions for the Non-Bankruptcy Business Lawyer*, 29 BUS. LAW. 729, 729 n.2 (1974).

72. 28 U.S.C. § 1481 (1982) (repealed 1984). "This jurisdictional grant empowers bankruptcy courts to entertain a wide variety of cases involving . . . claims based on state law as well as those based on federal law." *Marathon Pipe Line Co.*, 458 U.S. at 54.

73. *Marathon Pipe Line Co.*, 458 U.S. at 85 (quoting 28 U.S.C. § 1471(c) (Supp. IV 1976)) (internal quotation marks omitted).

74. *See* U.S. CONST. art. III, § 1; *Stern*, 131 S. Ct. at 2609.

75. *Marathon Pipe Line Co.*, 458 U.S. at 87.

contract action did not fall within the exception.[76] They further agreed that bankruptcy courts were not adjuncts to the district courts.[77] Justice Rehnquist's concurrence added that an Article III judge must adjudicate proceedings consisting of "the stuff of the traditional actions at common law tried by the courts at Westminster in 1789" brought within federal court jurisdiction.[78] Although subsequent courts have wrestled with whether the plurality or Justice Rehnquist's concurrence represented the holding of *Marathon*,[79] *Stern* applies both as precedent[80] but focuses more on the public rights exception.[81]

Following *Marathon*, the Supreme Court stayed its ruling and Congress eventually enacted BAFJA[82] to repeal all the bankruptcy jurisdiction provisions of the Reform Act.[83] BAFJA "established the current bankruptcy jurisdictional scheme."[84] Bankruptcy judges be-

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76. *See id.* at 67–68, 90–91.

77. *See id.* at 71–72, 81–86, *noted in Stern*, 131 S. Ct. at 2610 ("A full majority of Justices in *Northern Pipeline* also rejected the debtor's argument that the bankruptcy court's exercise of jurisdiction was constitutional because the bankruptcy judge was acting merely as an adjunct of the district court or court of appeals."). *But see* Meoli v. Huntington Nat'l Bank (*In re* Teleservices Grp.), 456 B.R. 318, 328 (Bankr. W.D. Mich. 2011) (insisting that room still exists, "even after *Stern* to consider further the appellant's argument in *Northern Pipeline* that a bankruptcy court can still enter at least some orders as if it were an independent legislative court").

78. *Marathon Pipe Line Co.*, 458 U.S. at 90.

79. *See* Jason C. Matson, *Running Circles Around Marathon? The Effect of Accounts Receivable as Core or Noncore Proceedings on the Article III Courts*, 20 EMORY BANKR. DEV. J. 451, 492–93 (2004) ("Almost every court maintaining accounts receivable are noncore inevitably cite to Marathon. Some of these courts rely on the plurality opinion by Justice Brennan to hold that accounts receivable are private rights, and therefore, Congress could not delegate authority to the bankruptcy court to conclude that an accounts receivable is a core proceeding. The other courts rely on Justice Rehnquist's state law rights test in determining that accounts receivable are state law claims, and therefore, bankruptcy courts cannot treat accounts receivable as core proceedings.").

80. *See Stern*, 131 S. Ct. at 2609 ("When a suit is made of the stuff of the traditional actions at common law tried by the courts at Westminster in 1789, . . . and is brought within the bounds of federal jurisdiction, the responsibility for deciding that suit rests with Article III judges in Article III courts." (quoting *Marathon Pipe Line Co.*, 458 U.S. at 90) (internal quotation marks omitted)); *id* at 2609–11 (analyzing *Marathon Pipe Line's* plurality opinion).

81. *Id.* at 2609–11. At different points during the legislative process, which resulted in the Reform Act, drafts did include providing bankruptcy judges with Article III protections. *See* Susan Block-Lieb, *What Congress Had to Say: Legislative History as a Rehearsal of Congressional Response to* Stern v. Marshall, 86 AM. BANKR. L.J. 55, 71 (2012).

82. See Massachusetts v. Dartmouth House Nursing Home, Inc., 726 F.2d 26, 28–30 (1st Cir. 1984), for a timeline of the events occurring post-*Marathon* but pre-BAFJA and a discussion of the confusion wrought. *See also* Masterson, *supra* note 43, at 103–04.

83. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 333. For a thorough consideration of BAFJA and the legislative process creating it, see L.T. Ruth Coal Co. v. Big Sandy Coal & Coke Co. (*In re* L.T. Ruth Coal Co.), 66 B.R. 753, 758–74 (Bankr. E.D. Ky. 1986).

84. *In re* Freeway Foods of Greensboro, Inc., 466 B.R. 750, 764 (Bankr. M.D.N.C. 2012).

came "judicial officers of the United States district court."[85] In contrast to the Reform Act, BAFJA granted the district courts original jurisdiction for all cases arising under, arising in, or related to the Code.[86] District court judges are authorized to refer any and all cases and proceedings under the Code to the bankruptcy courts of their district.[87] Bankruptcy judges, however, are not free to enter final judgments on all cases or proceedings referred by the district courts.[88] Preliminarily, the proceeding must "relate to" or have some conceivable effect on the bankruptcy case.[89] Moreover, the statutory ability to enter a final judgment depends on the core–noncore distinction. Bankruptcy courts may enter final judgments in core proceedings arising in or under the Code.[90] Section 157(b)(2) of Title 28 provides a non-exhaustive list of examples of core proceedings.[91] The list includes counterclaims by the estate against individuals filing proofs of claims, fraudulent conveyance proceedings, and turnover orders.[92] When confronted with a noncore proceeding, a bankruptcy judge "submit[s] proposed findings of fact and conclusions of law to the district court."[93] Although bankruptcy judges have less adjudicatory authority than they had under the Reform Act, BAFJA still augmented their authority when compared to the summary/plenary dichotomy applied by the 1898 Act.[94] Prior to *Stern*, most courts did not question the constitutionality of BAFJA.[95]

D. Stern v. Marshall

The landscape of bankruptcy courts' Constitutional Power shifted on June 23, 2011, when the Supreme Court decided *Stern*. The facts of *Stern* are interesting and could produce an article or perhaps a book

85. 28 U.S.C. § 152(a)(1) (2006).

86. *Id.* § 1334(b).

87. *Id.* § 157(a).

88. New Horizon of N.Y. LLC v. Jacobs, 231 F.3d 143, 150 (4th Cir. 2000).

89. *See, e.g.*, *id.* at 155; Wood v. Wood (*In re* Wood), 825 F.2d 90, 93 (5th Cir. 1987); Pacor, Inc. v. Higgins (*In re* Pacor, Inc.), 743 F.2d 984, 994 (3d Cir. 1984). Conversely, if a proceeding is not related, the bankruptcy court does not have any jurisdiction over the proceeding. § 1334(b).

90. § 157(b)(1). For a discussion of the history of § 157, see Arnold Print Works, Inc. v. Apkin (*In re* Arnold Print Works, Inc.), 815 F.2d 165, 166–67 (1st Cir. 1987).

91. § 157(b)(2).

92. *Id.* § 157(b)(2)(C), (E), (H).

93. *Id.* § 157(c)(1).

94. Meoli v. Huntington Nat'l Bank (*In re* Teleservices Grp.), 456 B.R. 318, 325 (Bankr. W.D. Mich. 2011).

95. *In re* Freeway Foods of Greensboro, Inc., 466 B.R. 750, 766 (Bankr. M.D.N.C. 2012). *But see* L.T. Ruth Coal Co. v. Big Sandy Coal & Coke Co. (*In re* L.T. Ruth Coal Co.), 66 B.R. 753, 796 (Bankr. E.D. Ky. 1986) ("This court is unable to find any case law or logic to support the conclusion that 28 U.S.C. § 157(b) is consistent with Article III of the Constitution.").

themselves.[96] Boiled down, the central question was whether the bankruptcy court could enter a final judgment on the estate's counterclaim for tortious interference with an expected gift following the creditor's filing of a proof of claim, which included a claim for defamation.[97] The Supreme Court found that the trustee's state-law-based counterclaim existed independently of federal bankruptcy law and would not be resolved as part of the claims allowance process.[98] Therefore, final judgment could not be entered by a non-Article III court and 28 U.S.C. § 157(b) could not constitutionally bestow adjudicatory authority on a bankruptcy court.[99]

Stressing a point first recited in *Marathon*, *Stern* found that Article I bankruptcy courts cannot enter final judgments in nonbankruptcy matters based on the common law or state law.[100] Thus, "Congress may not withdraw from judicial cognizance any matter which, from its nature, is the subject of a suit at the common law, or in equity, or admiralty."[101] State-law-created rights—such as the contract action in *Marathon* or the tort action in *Stern*—are private rights and do not fall within the public rights exception discussed below in Part V(A).[102] Lastly, the Court was unmoved by the pleas of the dissenters and Vickie Marshall that the case would unbalance the division of work between bankruptcy courts and district courts, as well as inject signifi-

96. For a discussion of the facts and procedural posture of *Stern*, see *In re* Safety Harbor Resort & Spa, 456 B.R. 703, 707–10 (Bankr. M.D. Fla. 2011).

97. Stern v. Marshall, 131 S. Ct. 2594, 2601 (2011). The defendant's tort claim dealt with a separate issue of bankruptcy court jurisdiction: jurisdiction over personal injury tort claims. *See* § 157(b)(2)(O), (b)(5). However, the defendant's constructive and actual consent allowed the Court to save clarification of this issue for another day. *In re Safety Harbor Resort & Spa*, 456 B.R. at 707–10.

98. *Stern*, 131 S. Ct. at 2618.

99. *See id.* at 2618–20.

100. *In re Freeway Foods of Greensboro, Inc.*, 466 B.R. at 767 (citing *Stern*, 131 S. Ct. at 2609).

101. *Stern*, 131 S. Ct. at 2609 (quoting Murray v. Hoboken Land & Improvement Co., 59 U.S. 272, 284 (1855)) (internal quotation marks omitted); *see* N. Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 70 n.25 (1982) (plurality opinion) (noting that the dissent agrees that Congress is the best body to determine whether there is a need for federal independent courts).

102. *Stern*, 131 S. Ct. at 2615; *see* Schoenthal v. Irving Trust Co., 287 U.S. 92, 94–95 (1932) ("Suits to recover preferences constitute no part of the proceedings in bankruptcy but concern controversies arising out of it . . . They may be brought in the state courts as well as in the bankruptcy courts."). This result was somewhat surprising considering two recent cases had expanded the public rights doctrine. *See* Commodity Futures Trading Comm'n v. Schor, 478 U.S. 833, 854 (1986); Thomas v. Union Carbide Agric. Prods. Co., 473 U.S. 568, 586 (1985). However, the Court's subsequent discussion of public rights in *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989), signaled another possible path. S. Elizabeth Gibson, *Jury Trials and Core Proceedings: The Bankruptcy Judge's Uncertain Authority*, 65 AM. BANKR. L.J. 143, 174 (1991) ("The fate of core jurisdiction thus may hinge on which line of authority the Supreme Court decides to follow."); *see also* Alec P. Ostrow, *Constitutionality of Core Jurisdiction*, 68 AM. BANKR. L.J. 91, 95–96 (1994).

cant uncertainty into the adjudicatory framework for bankruptcy proceedings.[103]

Stern created a two-prong test to decide whether a bankruptcy court has Constitutional Power over a core proceeding[104]: "whether the action at issue stems from the bankruptcy itself or would necessarily be resolved in the claims allowance process."[105] The test is disjunctive. If either prong is met, the bankruptcy court may enter a final judgment on that specific action.[106] If neither prong is satisfied, the bankruptcy court may only submit proposed findings of fact and conclusions of law to the district court.[107] This last assertion was more tenuous in the months immediately following *Stern* as courts were confronted with formulating a procedure for adjudicating proceedings that fell within the list of core proceedings but could not be adjudicated due to *Stern.* No provision was made for dealing with these "core but precluded"[108] proceedings.[109] Although bankruptcy courts have unanimously adopted the practice of submitting proposed findings of fact and conclusions of law to the district court,[110] the Ninth Circuit recently became the first circuit to recognize it.[111]

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103. *Stern*, 131 S. Ct. at 2618–20.

104. The *Stern* test is applied only to core proceedings. Schafer v. Nextiraone Fed., LLC, No. 1:12cv289, 2012 WL 2281828, at *5 (M.D.N.C. June 18, 2012).

105. *Stern*, 131 S. Ct. at 2618.

106. *Id.*

107. Paloian v. Am. Express Co. (*In re* Canopy Fin., Inc.), 464 B.R. 770, 774 (N.D. Ill. 2011) (noting that even though a bankruptcy court could not enter final judgment on a core claim, the district court was unwilling to "leav[e] [the proceedings] to occupy a virtual 'no man's land' on the statutory landscape" but not let the bankruptcy court treat the proceeding like a noncore proceeding). This proposition was disputed by at least one court in the early months following *Stern*. *See* Samson v. Blixseth (*In re* Blixseth), No. 09-60452-7, 2011 WL 3274042, at *12 (Bankr. D. Mont. Aug. 1, 2011) (holding that a bankruptcy court could not issue proposed findings of fact and conclusions of law because the court lacked jurisdiction over a core but unconstitutionally justiciable action), *amended by* 463 B.R. 896 (Bankr. D. Mont. 2012).

108. *See* Kirschner v. Agoglia (*In re* Refco Inc.), 461 B.R. 181, 186 (Bankr. S.D.N.Y. 2011) (coining the term "core but precluded").

109. *In re Blixseth*, 2011 WL 3274042, at *12 ("Unlike in non-core proceedings, a bankruptcy court has no statutory authority to render findings of fact and conclusions of law for core proceedings that it may not constitutionally hear.").

110. Courts have subsequently found that bankruptcy courts may constitutionally provide proposed findings of fact and conclusions of law for core claims that cannot be constitutionally adjudicated. *See* Deitz v. Ford (*In re* Deitz), 469 B.R. 11, 19–20 (B.A.P. 9th Cir. 2012) (listing cases). Moreover, the bankruptcy court for the District of Montana has responded to criticism by modifying its holding to allow for proposed findings of fact and conclusions of law. *See In re Blixseth*, 463 B.R. 896.

111. Exec. Benefits Ins. Agency v. Arkison (*In re* Bellingham Ins. Agency, Inc.), 702 F.3d 553, 565–67 (9th Cir. 2012). Although the Seventh Circuit appeared uncomfortable with allowing a bankruptcy court to submit proposed findings of fact and conclusions of law for a core but precluded proceeding, Ortiz v. Aurora Health Care, Inc. (*In re* Ortiz), 665 F.3d 906, 915 (7th Cir. 2011), it did refer the case back to the bankruptcy court without instructions to do nothing which

III. CONSTITUTIONAL JURISDICTION OF BANKRUPTCY COURTS: RIGHT TO A JURY TRIAL

The Seventh Amendment right to a jury trial in bankruptcy proceedings has a long and varied history.[112] The Seventh Amendment provides, "[i]n Suits at common law, . . . the right of trial by jury shall be preserved."[113] The goal of the Seventh Amendment is "to preserve the right to [a] jury trial as it existed in 1791" and to apply that right to actions analogous to those decided in the English law courts at the time of the Constitution's ratification.[114] The right to a jury trial attaches unless Congress constitutionally allows a non-Article III court to adjudicate the proceeding without a jury.[115] When addressing

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the Northern District of Illinois construed as tacit approval. *See* Gecker v. Flynn (*In re* Emerald Casino, Inc.), 467 B.R. 128, 132–33 (N.D. Ill. Jan. 31, 2012). Prior to *Stern*, the Fifth Circuit hinted that a core but precluded proceeding could be adjudicated by a bankruptcy court if it were subject to de novo review by a district court and did not require a jury trial. *Compare* McFarland v. Leyh (*In re* Tex. Gen. Petrol. Corp.), 52 F.3d 1330, 1337 (5th Cir. 1995) (hinting that de novo review by a district court is sufficient to allow a bankruptcy court to adjudicate a nonjury trial core but precluded action), *with In re* Clay, 35 F.3d 190, 194 (5th Cir. 1994) (disapproving of a bankruptcy court conducting jury trials even when subject to de novo review). For an interesting summary of the background of *Texas General*, which involved an original opinion issued by the Court of Appeals that was subsequently withdrawn because it could not coexist with *Clay*, see Leif M. Clark, *Bankruptcy*, 27 TEX. TECH. L. REV. 533, 539–40 (1996).

112. Much ink has been spilled analyzing whether the right to a jury trial attaches in bankruptcy proceedings, both generally and in core proceedings. *See, e.g.*, Denise M. Barton, *In re* Clay*: The Fifth Circuit Denies Bankruptcy Courts the Power to Conduct Jury Trials Without Consent of the Parties*, 69 TUL. L. REV. 1703 (1995); Gibson, *supra* note 102, at 174 (explaining inconsistent case law); G. Ray Warner, Katchen *Up in Bankruptcy: The New Jury Trial Right*, 63 AM. BANKR. L.J. 1 (1989).

113. U.S. CONST. amend. VII. The Supreme Court interprets the phrase "[s]uits at common law" to refer to "suits in which *legal* rights were to be ascertained and determined, in contradistinction to those where equitable rights alone were recognized, and equitable remedies were administered." Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 41 (1989) (quoting Parsons v. Bedford, 28 U.S. 433, 447 (1830)) (internal quotation marks omitted).

114. *Granfinanciera*, 492 U.S. at 41 (quoting Curtis v. Loether, 415 U.S. 189, 193 (1974)).

115. *Id.* at 50. Much confusion still exists surrounding the scope of the bankruptcy courts' power to conduct jury trials. A circuit split exists over whether a bankruptcy court may hold a jury trial. *Compare In re Clay*, 35 F.3d at 194 (construing BAFJA as not empowering bankruptcy judges to hold jury trials to avoid constitutional issue); Official Comm. of Unsecured Creditors v. Schwartzman (*In re* Stansbury Poplar Place, Inc.), 13 F.3d 122, 128 (4th Cir. 1993) (same); *In re* Grabill Corp., 967 F.2d 1152, 1158 (7th Cir. 1992) (same); Rafoth v. Nat'l Union Fire Ins. Co. (*In re* Baker & Getty Fin. Servs., Inc.), 954 F.2d 1169, 1173 (6th Cir. 1992) (relying on the BAFJA argument only); Kaiser Steel Corp. v. Frates (*In re* Kaiser Steel Corp.), 911 F.2d 380, 392 (10th Cir. 1990) (construing BAFJA as not empowering bankruptcy judges to hold jury trials to avoid constitutional issue); *and In re* United Mo. Bank of Kan. City, N.A., 901 F.2d 1449, 1456–57 (8th Cir. 1990) (same), *with* Ben Cooper, Inc. v. Ins. Co. of Pa. (*In re* Ben Cooper, Inc.), 896 F.2d 1394, 1403–04 (2d Cir. 1990) (allowing bankruptcy courts to conduct jury trials), *cert. granted*, 497 U.S. 1023, *vacated and remanded*, 498 U.S. 964, *reinstated on remand*, 924 F.2d 36 (2d Cir. 1991). Congress attempted to allow bankruptcy judges to conduct jury trials in cases where the district court designated the bankruptcy courts with that ability. 28 U.S.C. § 157(e) (2006). Even following this express grant from Congress, many courts are unwilling to allow

whether the right to a jury trial attaches to a cause of action, a three-part test is applied.[116] The first two steps are not part of the *Stern* test.[117] The third step mirrors the *Stern* test as the question is whether the claim stems from the bankruptcy itself or is necessarily adjudicated in the claims allowance process.[118] Analogous to *Stern's* guidance regarding interpretation of the breadth of Article III jurisdiction, the right to a jury trial "should be liberally construed."[119] Although the two case lines have traditionally been compartmentalized, *Stern's* reliance on the Seventh Amendment Case Line has imported this line into the Constitutional Adjudication Case Line. On a cautionary note, the right to a jury trial is narrower than the right to Article III adjudication because the right to a jury trial does not attach to a core equitable action, but a core equitable action will still require Article III adjudication if it does not satisfy either prong of the *Stern* test.[120] This Part will profile the four preeminent bankruptcy jury trial cases decided by the Supreme Court, the Seventh Amendment Case Line.

A. Schoenthal *and* Katchen

Schoenthal v. Irving Trust Co. held that the right to a jury trial attached to a counterclaim by an estate for preferential transfers against

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bankruptcy courts to hold jury trials. *See* Barton, *supra* note 112, at 1715 n.89 (listing cases). The power of bankruptcy judges to conduct jury trials is distinct from deciding whether the right to a jury trial attaches to an action that could be adjudicated in bankruptcy court. This Article will focus on the latter inquiry.

116. *Granfinanciera*, 492 U.S. at 42.

117. The first part requires categorizing the action as either legal or equitable under the standards of English courts prior to the merger of law and equity courts. *Id.* The second part categorizes whether the remedy sought is equitable or legal. *Id.* The second inquiry is more important. *Id.* This distinction is helpful considering the "anemic explanatory power of the first inquiry." *In re* Jensen, 946 F.2d 369, 371 (5th Cir. 1991).

118. Although *Granfinanciera* did not use the language "stems from the bankruptcy itself," it used the phrases "integral to the restructuring of debtor–creditor relations" and "integrally related to the reformation of debtor–creditor relations." *Granfinanciera*, 492 U.S. at 58, 60. Considering the use of each of these phrases as a limitation prior to enumerating the limitation of the claims allowance process, the author believes these three phrases all represent the same requirement. *See* Stern v. Marshall, 131 S. Ct. 2594, 2618 (2011); *Granfinanciera*, 492 U.S. at 58, 60; *cf.* Comm. of Unsecured Creditors of N.C. Hosp. Ass'n Trust Fund v. Mem'l Mission Med. Ctr., Inc. (*In re* N.C. Hosp. Ass'n Trust Fund), 112 B.R. 759, 762–63 (Bankr. E.D.N.C. 1990) (applying the two phrases in tandem for jury trial analysis). Sadly, the Supreme Court did not use either of the latter two phrases in any case except *Granfinanciera*.

119. Schoenthal v. Irving Trust Co., 287 U.S. 92, 94 (1932).

120. *See* Ahart, *supra* note 12, at 195, 200; Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 151 n.135. Especially prior to *Granfinanciera*, many courts folded the consideration of the *Stern* test into the first or second prong of the test. *See* Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 151 n.135.

a third party.[121] The trustee sued the defendants to recover allegedly preferential transfers of money made by the debtor.[122] Because the defendants had not filed a proof of claim, the claims allowance process was not implicated.[123] The Court found that preference actions did not stem from the bankruptcy itself because they were not part of bankruptcy proceedings at common law.[124] Hence, the preferences could not be summarily adjudicated by a bankruptcy referee without a jury trial.[125]

In *Katchen*, the Supreme Court first used the claims allowance process as a determinant of whether the right to a jury trial attaches to an action.[126] Unlike the defendants in *Schoenthal*, the defendant of the trustee's preference action in *Katchen* filed a proof of claim against the debtor's estate.[127] Although plenary jurisdiction and the accompanying right to a jury trial attached to the preference avoidance actions,[128] the filing of a proof of claim could vitiate that right.[129] The claims allowance process involved the bankruptcy referee's power to allow and disallow claims: "an adjudication of interests claimed in a *res*."[130] By filing a proof of claim, the creditor sought relief through a summary proceeding of the bankruptcy court.[131] Section 57(g) of the 1898 Act extended bankruptcy courts' summary jurisdiction to disallow a defendant's proof of claim if the creditor was found liable for a preference or fraudulent transfer, unless and until the amount of the preference was paid to the estate.[132] In short, when the adjudication of the proof of claim required adjudication of the estate's counterclaim, the filing of a proof of claim by the defendant converted the action from one requiring a plenary proceeding with an accompanying

121. 287 U.S. at 96–97.

122. *Id.* at 93. Because the court did not discuss a filing of a proof of claim by the defendants, we can assume that one was not filed and the claims allowance process was not implicated. *Granfinanciera*, 492 U.S. at 48.

123. This is not apparent from reading *Schoenthal*. However, both *Katchen* and *Granfinanciera* explained that the *Schoenthal* defendant had not filed a proof of claim. *Granfinanciera*, 492 U.S. at 58 (citing Katchen v. Landy, 382 U.S. 323, 336 (1966)).

124. *Schoenthal*, 287 U.S. at 94 n.1, 95.

125. *Id.* at 96.

126. 382 U.S. 323.

127. *Id.* at 325.

128. This is certainly true when the action seeks the return of money. *See Granfinanciera*, 492 U.S. at 46 n.5; *Schoenthal*, 287 U.S. at 94–95. *But see* McCoid, *supra* note 21, at 23–28. If the action were to seek recovery of a piece of real property, the availability of a plenary suit is more questionable. *See Granfinanciera*, 492 U.S. at 46 n.5; Resolution Trust Corp. v. Pasquariello (*In re* Pasquariello), 16 F.3d 525, 530–31 (3d Cir. 1994).

129. *Katchen*, 382 U.S. at 333 n.9.

130. *Id.* at 329 (quoting Gardner v. New Jersey, 329 U.S. 565, 574 (1947)).

131. *Id.* at 329–30.

132. *Id.* at 333–34; *see infra* Part IV(C)(1).

right to a jury trial into one that could be summarily adjudicated by a referee.[133]

B. Granfinanciera *and* Langenkamp

In the wake of *Marathon* and the enactment of BAFJA, the Supreme Court considered whether the right to a jury trial attached to a fraudulent transfer proceeding in *Granfinanciera, S.A. v. Nordberg*.[134] In *Granfinanciera*, the defendant was sued by the trustee for receipt of a fraudulent transfer from the debtor, but the defendant had not filed a proof of claim against the debtor's estate.[135] BAFJA designated fraudulent transfers as an example of core proceedings that a bankruptcy court could finally adjudicate, presumably without a jury.[136] Regardless, the right to a jury trial attached to the debtor's fraudulent transfer action.[137] In a discussion that would later be echoed with a slightly different focus by *Stern*, the Court explained that statutory jurisdiction bestowed by § 157 of the Code does not overcome constitutional deficiencies.[138] Congress's categorization of a fraudulent conveyance action as a core proceeding is not sufficient to bring it within the embrace of the public rights doctrine and strip the common-law right to a jury trial.[139] At bottom, a fraudulent conveyance action is a suit "to augment the bankruptcy estate" and does not stem from the bankruptcy itself.[140] Additionally, the Court relied upon both fraudulent transfer and preferential transfer cases.[141] As a result, the Court replicated the analysis used in *Schoenthal*, finding that the right to a jury trial attached to the fraudulent transfer action against a party who had not filed a proof of claim.[142]

In its latest bankruptcy jury trial decision, *Langenkamp v. Culp*, the Supreme Court reconciled *Katchen* and *Granfinanciera*.[143] When a creditor files a proof of claim, "it triggers the process of allowance and disallowance of claims, thereby subjecting [the creditor] to the bank-

133. *See Katchen*, 382 U.S. at 336.

134. Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 33 (1989).

135. *Id.* at 36.

136. 28 U.S.C. § 157(b)(2)(H) (2006); *Granfinanciera*, 492 U.S. at 50.

137. *Granfinanciera*, 492 U.S. at 60–61.

138. *Id.* at 58–59, 60–61.

139. *Id.* at 61 ("Congress cannot eliminate a party's *Seventh Amendment* right to a jury trial merely by relabeling the cause of action to which it attaches and placing exclusive jurisdiction in an administrative agency or a specialized court of equity.").

140. *See id.* at 57–58.

141. *See id.* at 57–60.

142. *Granfinanciera*, 492 U.S. at 58–59.

143. *See generally* Langenkamp v. Culp, 498 U.S. 42 (1990) (per curiam).

ruptcy court's equitable power."[144] This equitable power severed the right to a jury trial on the trustee's preference action because the creditor filed a proof of claim.[145] *Stern* dramatically increased the significance of the Seventh Amendment Case Line by incorporating relevant portions of its analysis as precedent for the Constitutional Adjudication Case Line.[146]

IV. THE CLAIMS ALLOWANCE PROCESS

The Constitutional Power of bankruptcy courts extends to actions that will necessarily be resolved as part of the claims allowance process, regardless of the consent of either a creditor or the estate. Although the claims allowance process was first employed by *Katchen*, its boundaries were only later explained in *Stern*. As a review of the § 502 claims allowance process, Bankruptcy Rule 3002(a) requires an unsecured prepetition creditor to file a proof of claim to receive a dividend from the estate.[147] When a creditor files a proof of claim pursuant to § 501(a), his claim must navigate the § 502 allowance process, including § 502(d).[148] The claims allowance process is implicated by both the analyses of the Constitutional Power and the right to a jury trial.[149] Because the Supreme Court has used this analysis when considering both Constitutional Power of bankruptcy courts and whether the right to jury trial attaches in bankruptcy court, the claims allowance process should have the same meaning in both analyses.[150] Moreover, pursuant to the canon of statutory interpretation of *ratio decidendi*, when a reason is given for a case's decision"—a *ratio decidendi*—it is authority in every other case in which that *ratio decidendi* is applicable."[151] According to *Stern*, if an action against a creditor who files a proof of claim must be decided as part of adjudicating the creditor's proof of claim, the bankruptcy court's Constitutional Power extends to the counterclaim as well as the proof of claim.[152] However, the claims allowance process has many wrinkles beyond the process outlined in *Stern*.

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144. *Id.* at 44 (quoting *Granfinanciera*, 492 U.S. at 58–59, 59 n.14) (internal quotation marks omitted).

145. *Id.* at 44–45.

146. *See generally* Stern v. Marshall, 131 S. Ct. 2594 (2011).

147. FED. R. BANKR. P. 3002(a).

148. *See generally* 11 U.S.C. §§ 501(a), 502(d) (2006).

149. *See Stern*, 131 S. Ct. at 2617–18; Katchen v. Landy, 382 U.S. 323, 329–30, 332–34 (1966).

150. *See Stern*, 131 S. Ct. at 2617–18; *Katchen*, 382 U.S. at 329–30, 332–34.

151. *E.g.*, United States v. Tyler, 466 F.2d 920, 926 (9th Cir. 1972) (Duniway, J., concurring and dissenting).

152. *See generally Stern*, 131 S. Ct. 2594.

This Part will first explain the basic claims allowance process as outlined in *Katchen* and *Stern.* It will then turn to § 502(d), a subsection at the center of *Katchen* that eases satisfaction of *Stern's* requirement that all legal and factual issues must be adjudicated as part of ruling on the defendant's proof of claim. Next, it analyzes whether a third party's action setoff, reclamation, and recoupment are part of the claims allowance process, even though they do not always require a proof of claim. It then focuses on whether administrative expenses should be part of the claims allowance process even though they are allowed through a different process under a different subsection of the Code. Further uncertainty exists over the application of § 502(d) to administrative expenses. It then analyzes whether informal proofs of claim fit within the claims allowance process. Lastly, it favors extending the claims allowance process to place the estate on equal footing with creditors.

A. *Pre-1898 Act Illustrations*

Bankruptcy proceedings "provide speedy proceedings, and the ascertainment and adjustment of all claims and rights in favor of or against the bankrupt's estate."[153] In *Wiswall v. Campbell*, Chief Justice Waite introduced the view that creditors paid a price for this swiftness and convenience as "a creditor who offers proof of his claim, and demands its allowance, subjects himself to the dominion of the court, and must abide the consequences."[154] The consequence and remedy to which *Wiswall* alluded was the claims allowance process prescribed by the 1867 Act.[155] Eighty years later, this view was known as "traditional" and citation was unnecessary.[156] One hundred and thirty-five years later, *Stern* still relied upon the same rationale.[157]

B. Katchen *and* Stern

Although *Katchen* coined the term "claims allowance process,"[158] as *Granfinanciera* and *Langenkamp* recognized, the Supreme Court did not explain the parameters of the term until *Stern. Katchen* relied upon *Wiswall's* declaration that "he who invokes the aid of the bankruptcy court by offering a proof of claim and demanding its allowance

153. *Ex parte* Christy, 44 U.S. (1 How.) 292, 314 (1845) (Story, J.).

154. Wiswall v. Campbell, 93 U.S. 347, 351 (1876).

155. *Id. Wiswall* gave a summary of the process at this point but also referred back to the more detailed, section by section, explanation earlier in the opinion. *See id.* at 349–51.

156. Gardner v. New Jersey, 329 U.S. 565, 573 (1947).

157. *Stern*, 131 S. Ct. at 2616 (citing Katchen v. Landy, 382 U.S. 323, 333 (1966)).

158. This phrase was originally known as the "process of allowance and disallowance of claims." *Katchen*, 382 U.S. at 336.

must abide the consequences of that procedure."[159] It then expounded on the potential consequences, including summary adjudication of both objections to the proof of claim and actions for affirmative relief, which would also be decided as part of adjudicating the proof of claim.[160] The Court, however, "intimate[d] no opinion concerning whether [the referee would have had] summary jurisdiction to adjudicate a demand by the trustee for affirmative relief, all of the substantial factual and legal bases for which ha[d] not been disposed of in passing on objections to the [creditor's proof of] claim."[161] Neither *Granfinanciera* nor *Langenkamp* analyzed the degree of overlap necessary for a counterclaim against a creditor to fit within the claims allowance process.[162] Faced with this ambiguity, some courts viewed the filing of a proof of claim as sufficient to waive the right to a jury trial regardless of the lack of factual or legal overlap.[163] In contrast, other courts found that an estate's counterclaim for affirmative relief must be completely decided as part of adjudicating the creditor's proof of claim to waive the litigant's right to a jury trial.[164]

Stern finally explained that the boundaries of the claims allowance process covered affirmative actions only if the action would necessarily be decided as part of deciding the creditor's proof of claim.[165] In *Stern*, a factual overlap existed between deciding the creditor's proof of claim, including his claim for defamation, and deciding the debtor's counterclaim for tortious interference with an expected gift.[166] The overlap, however, was far from complete, as the Court would need to decide at least two thorny legal issues that were present in only the

159. *Id.* at 333 n.9 (citations omitted).

160. *Id.* at 337–38.

161. *Id.* at 333 n.9. As contemporary commentators observed, "[i]t is difficult to see any illumination in the still dark area of non-57g counterclaims." Rochelle & King, *supra* note 62, at 680.

162. *See* Billing v. Ravin, Greenberg & Zackin, P.A., 22 F.3d 1242, 1248 (3d Cir. 1994) ("[*Katchen*] did not further define the scope of the allowance and disallowance process.").

163. *See, e.g.*, Bankr. Servs., Inc. v. Ernst & Young (*In re* CBI Holding Co.), 529 F.3d 432, 461 n.12, 464 (2d Cir. 2008) (explaining that the creditor's fee claims are part of the entire claim against the debtor); Humboldt Express, Inc. v. Wise Co. (*In re* Apex Express Corp.), 190 F.3d 624, 631 n.7 (4th Cir. 1999) (noting the creditors consent to the bankruptcy court's jurisdiction upon the filing of a proof of claim); *Billing*, 22 F.3d at 1249 ("*Langenkamp* seems to formulate a bright-line rule, holding that creditors who file proofs of claim against the estate are not entitled to a jury trial on matters affecting the allowance of those claims.").

164. *See, e.g.*, Germain v. Conn. Nat'l Bank, 988 F.2d 1323, 1327, 1329 (2d Cir. 1993); Redington v. Touche Ross & Co., 612 F.2d 68, 73 (2d Cir. 1979).

165. *See* Stern v. Marshall, 131 S. Ct. 2594, 2617–18 (2011).

166. *Id.* at 2617.

debtor's counterclaim.[167] "[A]t the outset of the claims-disallowance process, [the court lacked] reason to believe that the process of adjudicating [the] proof of claim would necessarily resolve" the common-law claims.[168] Following *Stern*, the claims allowance process will allow constitutional adjudication by a bankruptcy court only when ruling on a creditor's proof of claim will necessarily resolve all the legal and factual issues of the estate's action against the creditor.[169]

In the wake of *Stern*, at least one case has analyzed the degree of overlap necessary to satisfy *Stern's* requirement of necessary resolution by the claims allowance process.[170] The overlap required to be necessarily resolved by the claims allowance process was found analogous to the test applied when a defendant seeks to remove a proceeding to federal court pursuant to federal question jurisdiction.[171] A plaintiff may remove a proceeding only if the plaintiff's right to relief "*necessarily depends on* a question of federal law."[172] In other words, the plaintiff will be successful only if "*every* legal theory supporting the claim requires the resolution of a federal issue."[173] Applying this test to the claims allowance process, if there is any theory that adjudicates a creditor's proof of claim without completely adjudicating the estate's counterclaim, the claims allowance process is not sufficiently implicated.[174]

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167. *Id.* (explaining that the elements of the action and availability of punitive damages for tortious interference with an expected gift under Texas law were undecided at the time of the bankruptcy court's judgment).

168. Waldman v. Stone, 698 F.3d 910, 921 (6th Cir. 2012) (quoting *Stern*, 131 S. Ct. at 2617) (internal quotation marks omitted).

169. *Stern*, 131 S. Ct. at 2618; *see* Tolliver v. Bank of Am. (*In re* Tolliver), 464 B.R. 720, 736 (Bankr. E.D. Ky. 2012) (explaining that the court in *Stern* looked at not only the "factual overlap of the claim resolution and the counterclaim, but also the legal elements which must be determined to resolve the claim and the counterclaim and the remedies sought by the counterclaim and the impact on the claims allowance process"). This limitation is a significant change from previous practices where "[c]ourts have consistently held that counterclaims and defenses filed in an adversary proceeding seeking affirmative relief from a debtor's estate constitute[d] claims against the bankruptcy estate that divest the defendant of the right to a jury trial" because the claims allowance process is invoked. Gecker v. Marathon Fin. Ins. Co. (*In re* Auto Prof'ls, Inc.), 389 B.R. 621, 629 (Bankr. N.D. Ill. 2008).

170. Black, Davis & Shue Agency, Inc. v. Frontier Ins. Co. in Rehab. (*In re* Black, Davis & Shue Agency, Inc.), 471 B.R. 381, 401–02 (Bankr. M.D. Pa. 2012).

171. *Id.* at 402.

172. *Id.* (quoting Dixon v. Coburg Dairy, Inc., 369 F.3d 811, 816 (4th Cir. 2004)) (internal quotation marks omitted).

173. *Id.* (quoting *Dixon*, 369 F.3d at 816).

174. *Id.* Other courts have been more lenient. *See* Spanish Palms Mktg., LLC v. Kingston (*In re* Kingston), No. 11-40128-JDP, 2012 WL 632398, at *2 (Bankr. D. Idaho Feb. 27, 2012) (noting that issues "intricately melded" with determining proof of claim could be adjudicated pursuant to the claims allowance process). The proper procedure for a bankruptcy court to undertake in determining whether an action will be necessarily adjudicated is uncertain. The Sixth Circuit

C. *Beyond* Stern

This Subpart considers the boundaries of the claims allowance process beyond the answers provided by the Seventh Amendment Case Line and Constitutional Adjudication Case Line.

1. § 502(d)

Section 502(d) eases satisfaction of the second prong of the *Stern* test by requiring that certain causes of action by the estate against a creditor will be completely adjudicated as part of ruling on the creditor's proof of claim, regardless of a lack of complete factual or legal overlap. As noted above, *Stern* allows a bankruptcy court to adjudicate a state-law-based counterclaim against a creditor only when the ruling on the creditor's proof of claim will dispose of all factual and legal issues presented by the counterclaim.[175] Although the avoidance claims encompassed in § 502(d) are found in the Code, first *Schoenthal*[176] (§ 547 preference) and then *Granfinanciera*[177] (fraudulent conveyance) ruled that these actions are equivalent to state-law-based actions. Section 502(d) makes the lack of complete legal and factual overlap irrelevant because the avoidance action must be adjudicated before the proof of claim is allowed. Hence, the avoidance action is necessarily resolved as part of the claims allowance process. This power is not uncontroverted. The boundaries of § 502(d) have never been truly defined.[178] Moreover, Professor Brubaker asserts that § 502(d) is applicable only within the traditional notions of summary jurisdiction under the 1898 Act.[179] Although some evidence supports his view, the claims allowance process in general has always been defined by the sovereign and adjudicated by a non-Article III tribunal.[180] Therefore, unlike other areas of bankruptcy, Congress may reasonably define the process as it desires.

Section 502(d) currently disallows the claims of a creditor from whom "property is recoverable under section 542, 543, 550, or 553 of [the Code] or that is a transferee of a transfer avoidable under section 522(f), 522(h), 544, 545, 547, 548, 549, or 724(a) of [the Code]" until

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recently opined that it did not "believe that *Stern* requires a court to determine, in advance, which facts will ultimately prove strictly necessary to resolve a creditor's proof of claim." Onkyo Eur. Elecs. GmbH v. Global Technovations Inc. (*In re* Global Technovations Inc.), 694 F.3d 705, 722 (6th Cir. 2012).

175. *See supra* notes 165–69 and accompanying text.

176. Schoenthal v. Irving Trust Co., 287 U.S. 92, 94–95 (1932).

177. Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 56 (1989).

178. *See* Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 155–56.

179. *Id.*

180. *Id.* at 125–26.

the transfers are surrendered to the estate.[181] According to the legislative history, it "requires disallowance of a claim of a transferee of a voidable transfer in toto if the transferee has not paid the amount or turned over the property received as required under the sections under which the transferee's liability arises."[182] *Stern's* explanation of the disallowance procedure of § 502(d) not only distinguished a preference from Vickie's counterclaim, but also reaffirmed the constitutionality of the procedure itself.[183] As the following sections illustrate, § 502(d) plays a large but ill-defined role in the claims allowance process. However, whether it is actually part of the claims allowance process is still uncertain.

At first glance, *Katchen* seems to directly support the proposition that the claims allowance process encompasses all objections to claims pursuant to § 502(d). The Court relied upon § 57(g), the analog to § 502(d) under the 1898 Act, and did not analyze the breadth of overlap between the estate's preference action and the creditor's proof of claim:

> Unavoidably and by the very terms of the Act, when a bankruptcy trustee presents a [§ 57(g)] objection to a claim, the claim can neither be allowed nor disallowed until the preference matter is adjudicated. The objection under [§ 57(g)] is, like other objections, part and parcel of the allowance process and is subject to summary adjudication by a bankruptcy court. This is the plain import of [§ 57] and finds support in the same policy of expedition that under-

181. 11 U.S.C.A. § 502(d) (West 2006). "The twin aims of section 502(d) are to assure an equality of distribution of the assets of the bankruptcy estate and to have the coercive effect of insuring compliance with judicial orders." Enron Corp. v. Springfield Assocs., LLC (*In re* Enron Corp.), 379 B.R. 425, 435 (S.D.N.Y. 2007) (quoting Campbell v. United States (*In re* Davis), 889 F.2d 658, 661, 662 (5th Cir. 1989)) (internal quotation marks omitted). A split of authority exists over whether a § 502(d) objection requires a prior adjudication of the avoidance action. *Compare* Enron Corp. v. Ave. Special Situations Fund II, LP (*In re* Enron Corp.), 340 B.R. 180, 210 (Bankr. S.D.N.Y. 2006) (failing to dismiss a § 502(d) objection even though the preference had not been adjudicated), *vacated sub nom. In re Enron Corp.*, 379 B.R. 425, *with* Giuliano v. Mitsubishi Digital Elecs. Am., Inc. (*In re* Ultimate Acquisition Partners, LP), No. 11-10245, 2012 WL 1556098, at *3 (Bankr. D. Del. May 1, 2012) ("A debtor or trustee wishing to avail itself of the benefits of section 502(d) must first obtain a judicial determination on the preference complaint." (quoting *In re* Lids Corp., 260 B.R. 680, 684 (Bankr. D. Del. 2001)) (internal quotation marks omitted)).

182. H.R. REP. No. 95-595, at 354 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6310 (emphasis added). Section 502(d) states, in relevant part, that "the court shall disallow any claim of any entity from which property is recoverable under section 542, 543, 550, or 553 of this title or that is a transferee of a transfer avoidable under section 522(f), 522(h), 544, 545, 547, 548, 549, or 724(a) of this title, unless such entity or transferee has paid the amount, or turned over any such property, for which such entity or transferee is liable under section 522(i), 542, 543, 550, or 553 of this title." § 502(d).

183. Stern v. Marshall, 131 S. Ct. 2594, 2616 (2011).

> lies the necessity for summary action in many other proceedings under the Act.[184]

The scope of § 57(g), however, was not settled at the time *Katchen* was decided, and the Court declined to rule on whether an objection applied to all the claims of a creditor.[185] In essence, can a creditor who is liable for an avoidable transfer surrender one claim and pursue the rest? Or, are all creditors' claims disallowed unless the preference is paid? On the one hand, if every claim is a separate unit, creditors will attempt to split claims, surrender the amount closest to the value of the avoidable transfer under § 502(d), and then file the higher valued claims for face value without fear of liability.[186] The advantage of surrendering a single claim instead of paying the disputed funds to the estate is that, in most cases, the creditor would not be paid in full on its claim, a discount known as bankruptcy dollars.[187] In contrast, a surrendered transfer would not be discounted. To stymie this strategic behavior, the majority of courts at the time *Katchen* was decided would not allow any of a creditor's claims until the entire voidable transfer was surrendered.[188] On the other hand, transactions between the debtor and creditor may in fact be separate, and failing to separate them can cause unfair hardship.[189] Regardless of the ambiguity in the scope of § 502(d), bankruptcy courts both before and after *Stern* have found that a voidable transfer or preference, together with the defendant's filing of a proof of claim, disallows all of the creditor's claims unless and until the creditor pays or surrenders the avoidable transfer.[190] As *Katchen* explained, "the language of [§ 57(g)], it will be ob-

184. Katchen v. Landy, 382 U.S. 323, 330–31 (1966).

185. *Id.* at 330 n.5. The Collier on Bankruptcy section cited by *Katchen* noted the problem attendant to interpreting § 502(d). *Id.* (citing 3 LAWRENCE P. KING, COLLIER ON BANKRUPTCY ¶ 57.19[3.2] (14th ed. 1964)).

186. *Katchen*, 382 U.S. at 330–31 (citing 3 KING, *supra* note 185). For example, when a creditor has one large claim for $1,000,000 and a looming preference action for $250,000, the creditor would prefer to split the claim into a $740,000 and a $260,000 claim because the creditor can surrender the $260,000 claim, forego litigation on the preference action and its accompanying expense, and not worry about preference liability for the $740,000 claim.

187. *See* Jay Lawrence Westbrook, *The Commission's Recommendations Concerning the Treatment of Bankruptcy Contracts*, 5 AM. BANKR. INST. L. REV. 463, 466 & n.23 (1997). As Professor Westbrook explains, the amount of discount applied dramatically influences the rational calculations of the parties. *Id.*; *see, e.g.*, Enron Corp. v. Ave. Special Situations Fund II, LP (*In re* Enron Corp.), 340 B.R. 180, 189 (Bankr. S.D.N.Y. 2006), *vacated sub nom.* Enron Corp. v. Springfield Assocs., LLC (*In re* Enron Corp.), 379 B.R. 425 (S.D.N.Y. 2007).

188. *See Katchen*, 382 U.S. at 330 n.5 (citing 3 KING, *supra* note 185).

189. *See* 3 KING, *supra* note 185.

190. *E.g.*, Parker N. Am. Corp. v. Resolution Trust Corp. (*In re* Parker N. Am. Corp.), 24 F.3d 1145, 1149 (9th Cir. 1994); Glinka v. Abraham & Rose Co., No. 2:93-CV-291, 1994 WL 905714, at *11 (D. Vt. June 6, 1994); *see In re* KB Toys, Inc., 470 B.R. 331, 335–36 (Bankr. D. Del. 2012); Burns v. Dennis (*In re* Se. Materials, Inc.), 467 B.R. 337, 349–50 (Bankr. M.D.N.C. 2012); West

served, is concerned with creditors rather than claims and thus contemplates that allowance of a claim may be conditioned on surrender of preferences received with respect to transactions unrelated to the claims."[191] This is the better view. Returning to *Wiswall*, the Supreme Court has observed that Congress has set the consequences of invoking the claims allowance process.[192] The legislative history, as noted above, further suggests that § 502(d) should halt allowance of all the claims of a creditor until the creditor pays or surrenders the value of the preference.[193]

The biggest issue with reliance on *Katchen's* use of § 502(d) as part of the claims allowance process is *Langenkamp's* failure to cite that section, even though it involved the same issue.[194] Professor Brubaker attempts to bridge this gap by finding that the Supreme Court has constitutionalized the summary/plenary dichotomy.[195] Brubaker posits that the 1898 Act had already categorized preference and fraudulent conveyance actions against a creditor as summary proceedings.[196] Thus, the use of § 57(g) and § 502(d) is unnecessary. When suing a creditor for a preference, the proceeding would have been summarily adjudicated under the 1898 Act but will now fall analogously within the Constitutional Power of bankruptcy courts.[197]

Brubaker's analysis of § 502(d) is incomplete because he does not consider the historical role of non-Article III tribunals in adjudicating the claims allowance process as delineated by the legislature. Brubaker correctly states that "adjudication of a preference suit against a creditor was categorized as a summary proceeding under the 1898 Act."[198] This categorization was cemented only by *Katchen*, however, as "it must be conceded that the Bankruptcy Act does not in express terms confer summary jurisdiction to order claimants to surrender preferences."[199] *Katchen* held that summary jurisdiction extends to

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v. Freedom Med., Inc. (*In re* Apex Long Term Acute Care–Katy, LP), 465 B.R. 452, 464–65 (Bankr. S.D. Tex. 2011); Gugino v. Canyon Cnty. (*In re* Bujak), No. 10-03569-JDP, 2011 WL 5326038, at *3 (Bankr. D. Idaho Nov. 3, 2011); *In re* Mid Atl. Fund, Inc., 60 B.R. 604, 609 (Bankr. S.D.N.Y. 1986).

191. *Katchen*, 382 U.S. at 330 n.5.

192. Wiswall v. Campbell, 93 U.S. 347, 350 (1876).

193. H.R. REP. NO. 95-595, at 354 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6310.

194. The Tenth Circuit noted that § 502(d) had been applied to disallow the claims of the creditors. Langenkamp v. Hackler (*In re* Republic Trust & Sav. Co.), 897 F.2d 1041, 1045 n.4 (10th Cir. 1990), *rev'd sub nom.* Langenkamp v. Culp, 498 U.S. 42 (1990) (per curiam).

195. Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 155–56.

196. *Id.* at 155.

197. *Id.* at 168–69.

198. *Id.* at 155.

199. *See* Katchen v. Landy, 382 U.S. 323, 328 (1966).

cover a preference action against a creditor by relying on two strings of authority, not the grant of summary jurisdiction itself. First, *Katchen* relied upon pre-1898 Act cases examining the power to adjudicate claims through the lens of statutory construction,[200] and second, the § 57(g) analysis was "[c]ritical to the Court's decision."[201] Therefore, one, the other, or both strains of authority were necessary to sustain *Katchen's* holding.[202] Brubaker cogently argues that statutory construction decisions are now binding precedent for the constitutional adjudication analysis because *Stern* relied upon the portions of *Katchen* applying them.[203] Accordingly, the codification of § 502(d) is unnecessary and represents a red herring in the search for constitutional boundaries. Professor Brubaker is aided by *Stern's* comment that Vickie Marshall's counterclaim fell within the grant of statutory jurisdiction yet could not be constitutionally adjudicated.[204] Therefore, he reasons that the expansive jurisdiction over a category of state-law-based counterclaims provided by § 502(d) cannot stand on codification alone.[205] If Brubaker is correct, § 502(d) may not set the boundaries of the claims allowance process, and only what traditionally encompassed the claims allowance process under the summary/plenary dichotomy falls within bankruptcy courts' Constitutional Power.

Unlike 28 U.S.C. § 157(b)(2)(C), the provision at issue in *Stern*, § 502(d), is part of the claims allowance process. Returning to *Wiswall* and *Katchen*, Congress has the power to delineate the claims allowance process without augmentation from the public rights exception.[206] *Stern* itself found that if an action is necessarily resolved as part of the claims allowance process, it falls within a bankruptcy

200. *Id.* at 329–30. Brubaker correctly notes that these cases are now binding authority on the Article III issue. Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 156–57.

201. Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 154.

202. Although *Stern* cites § 502(d) in its analysis of *Katchen*, it does not analyze whether it was a necessary consideration. Stern v. Marshall, 131 S. Ct. 2594, 2616 (2011).

203. Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 157.

204. *Stern*, 131 S. Ct. at 2608 ("Although we conclude that § 157(b)(2)(C) permits the Bankruptcy Court to enter final judgment on Vickie's counterclaim, Article III of the Constitution does not."). *Stern* did not limit or change the statutory jurisdiction inquiry. *See also* Rentas v. Claudio (*In re* Garcia), 471 B.R. 324, 329 (Bankr. D.P.R. 2012) ("In summary, when considering their authority to issue final orders, bankruptcy courts must first consider whether they have the statutory authority to issue a final order in a matter before them. . . . *Stern v. Marshall* . . . further mandates that when doing so, a bankruptcy court must first consider whether it has the necessary statutory authority and if it does it must then consider if it has the constitutional authority to finally adjudicate the dispute.").

205. *See* Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 176–78.

206. The public rights exception is another option for allowing § 502(d) to apply beyond its roots in the summary/plenary dichotomy of the 1898 Act. *See* Ostrow, *supra* note 102, at 107.

judge's Constitutional Power.[207] The allowance and disallowance of claims was within the bankruptcy commissioner's jurisdiction in England at the time of the founding,[208] and it has been set forth in each of the federal bankruptcy statutes.[209] *Stern* did not define the claims allowance process because it is a statutory creation and Congress can reasonably delineate its parameters.[210] As part of the claims allowance process, § 502(d) objections are within the Constitutional Power of bankruptcy judges regardless of the historical boundaries applied under the 1898 Act.

2. Reclamation

A creditor's claim for reclamation should invoke the claims allowance process as outlined in *Stern*. Section 546(c) provides a seller with a right to reclaim goods sold to the debtor in the ordinary course of the seller's business if the debtor was insolvent when it received the goods and the receipt of the goods occurred within forty-five days before the petition date.[211] The seller must also make a written demand for the goods within certain temporal parameters.[212] If a seller meets these requirements, the seller may reclaim the goods even when the estate possesses an action against the seller for avoiding a fraudu-

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207. *Stern*, 131 S. Ct. at 2620.

208. "Bankruptcy is entirely a creation of statute law. . . . Early statutes were intended to secure the property and assets of the bankrupt and distribute them ratably between his creditors." W.J. Jones, *The Foundations of English Bankruptcy: Statutes and Commissions in the Early Modern Period*, *in* 69 TRANSACTIONS OF THE AM. PHIL. SOC'Y 1, 8 (1979) (citations omitted); *see also* 2 WILLIAM BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND 479 (1800) (noting that bankruptcy proceedings at common law "depend[ed] entirely on the [s]everal [s]tatutes of bankruptcy"); Plank, *supra* note 22, at 569, 574, 587–88.

209. 11 U.S.C. § 502 (2006); Bankruptcy Act of 1898, ch. 541, § 57, 30 Stat. 544 (repealed 1978); Act of Mar. 2, 1867, ch. 176, § 19, 14 Stat. 517 (repealed 1878); Act of Aug. 19, 1841, ch. 9, §§ 5, 10, 5 Stat. 440 (repealed 1843); Act of Apr. 4, 1800, ch. 19, §§ 2, 29, 37, 39, 2 Stat. 19 (repealed 1803); Plank, *supra* note 22, at 569, 606–10. Professor Ferriell makes an important point that § 502(b)(1) necessarily applies rules of decision outside of the Code as part of the allowance of claims. Jeffrey T. Ferriell, *Constitutionality of the Bankruptcy Amendments and Federal Judgeship Act of 1984*, 63 AM. BANKR. L.J. 109, 142–43 (1989). However, *Stern* did not distinguish between the rules of decision applied as part of the claims allowance process. *Stern*, 131 S. Ct. at 2618. Instead, we can only assume that because an action must be necessarily resolved by the claims allowance process to satisfy that prong, the technique of looking beneath the action should not be applied to the claims allowance process.

210. *Cf.* 2 BLACKSTONE, *supra* note 208, at 479 (noting that bankruptcy proceedings at common law "depend[ed] entirely on the [s]everal [s]tatutes of bankruptcy").

211. § 546(c)(1).

212. *Id.* § 546(c)(1)(A)–(B). The demand must be made within forty-five days of the debtor's receipt of the goods. *Id.* § 546(c)(1)(A). However, if the petition date is within the forty-five day period, the seller has twenty days following the petition date to make the demand. *Id.* § 546(c)(1)(B).

lent transfer, preferential transfer, or post-petition transfer, or it could invoke its strong-arm power.[213]

Almost eighty years before *Stern*, *Daniel v. Guaranty Trust Co.* limited the summary jurisdiction of bankruptcy referees over an estate's counterclaims against a reclaiming seller.[214] Prior to *Daniel*, many courts held that a reclaiming seller's filing of a petition for reclamation constituted consent to the bankruptcy court's summary adjudication of all issues, including unrelated affirmative actions by the estate.[215] In *Daniel*, the trustee attempted to prosecute a turnover action against the reclaiming seller that was not factually related to the reclamation claim.[216] The Supreme Court found that the referee did not have jurisdiction over the turnover action "unless [the reclaiming seller] by filing its petition for reclamation entered its general appearance and in effect consented to submit itself to summary proceedings before that officer in respect of matters having no immediate relation to the claim which it had presented."[217] Although *Daniel* employed the consent rationale used prior to *Katchen*, reclamation easily fits within the claims allowance process. A claim for reclamation should be treated like a proof of claim as it seeks receipt of a portion of the bankruptcy res, and a bankruptcy court employs the process outlined in § 546(c) to decide whether the property is subject to reclamation.[218] Considering *Stern* has prescribed that an estate's action must be necessarily adjudicated as part of ruling on a proof of claim to fit within the claims allowance process, the same test should prescribe the necessary degree of overlap between a reclamation claim and an action by the estate.[219] If a state-law-based counterclaim can be adjudicated as part of the process of ruling on the claim for reclamation, the counterclaim would be necessarily resolved by the claims allowance process.

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213. *Id.* § 546(c)(1). The reach of § 502(d) does not extend to reclamation claims. *See id.* § 502(d).

214. *See generally* Daniel v. Guaranty Trust Co. of N.Y., 285 U.S. 154 (1932). *Daniel* also parallels *Stern* in noting that efficiency is not a sufficient reason to increase the jurisdiction of bankruptcy courts. *Compare Daniel*, 285 U.S. at 162 (noting speedy administration is not enough to increase jurisdiction), *with Stern*, 131 S. Ct. at 2619–20 (explaining that courts defer to Congress's decision to avoid encroaching on Article III judges).

215. *Consent to Summary Jurisdiction*, *supra* note 52, at 473–74 & n.38 (citing *In re* Barnett, 12 F.2d 73, 81 (2d Cir. 1926)); *In re* Pa. Coffee Co., 8 F.2d 98 (W.D. Pa. 1925).

216. *Daniel*, 285 U.S. at 158–59.

217. *Id.* at 162.

218. Rochelle & King, *supra* note 62, at 670 n.8.

219. Section 502(d) does not cover reclamation claims. *See* 11 U.S.C.A. § 502(d) (West 2006). Therefore, the overlap between the estate's action and the creditor's proof of claim prescribed by *Stern* must be satisfied.

3. Setoff

Setoff invokes the claims allowance process because a creditor must possess an allowed claim to offset its debt to the estate.[220] Similar to reclamation, setoff's origins predate the Code and the 1898 Act.[221] In bankruptcy, setoff is governed by § 553 of the Code, which allows a creditor to cancel a debt owed by the creditor to the estate against the creditor's claim if both debts arose prior to the commencement of bankruptcy and the debts are mutual.[222] Mutuality is established when the debt is "between the same parties standing in the same capacity."[223] Moreover, one further requirement is that the mutual debts arise from extrinsic or unrelated transactions.[224] Yet, "[§] 553 does not create a right to setoff."[225] Instead, the underlying state law must allow the use of setoff rights while § 553 merely adds requirements that must be satisfied in order to apply the setoff rights in bankruptcy.[226]

"Strictly speaking, a set-off is not a [defense]."[227] This distinction distinguishes setoff from recoupment and explains why setoff requires the application of the claims allowance process while recoupment does not. Setoff comes in two flavors: (1) if a creditor's claim is greater than the debt owed to the estate, the setoff is considered a counterclaim[228] and (2) if the creditor's claim is less than the debt owed to the estate, setoff is characterized as an affirmative defense.[229]

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220. *Id.* § 553(a)(1).

221. "[T]he remedy by set-off was unknown at common law, but is a creature of the statute." THOMAS W. WATERMAN, A TREATISE ON THE LAW OF SET-OFF, RECOUPMENT, AND COUNTER-CLAIM 10 (Baker, Voorhis & Co. eds., 1869). It also appeared far earlier on the equity side but it was limited to dealings where "it appeared to have been the intention of the parties that one debt should be set against the other." *Id.* at 18. The lack of common law heritage should not be construed as indicating setoff has modern origins considering "[t]he historical antecedent of the doctrine of setoff dates back to the Roman Empire." Campbell v. United States (*In re* Davis), 889 F.2d 658, 661 n.5 (5th Cir. 1989).

222. *E.g.*, Conoco, Inc. v. Styler (*In re* Peterson Distrib., Inc.), 82 F.3d 956, 959 (10th Cir. 1996).

223. *E.g.*, Farmers Home Admin. v. Buckner (*In re* Buckner), 218 B.R. 137, 145 (B.A.P. 10th Cir. 1998).

224. United Structures of Am., Inc. v. G.R.G. Eng'g, S.E., 9 F.3d 996, 998 (1st Cir. 1993).

225. Alexander & Jones v. Sovran Bank, N.A. (*In re* Nat Warren Contracting Co.), 905 F.2d 716, 718 (4th Cir. 1990) (quoting Durham v. SMI Indus. Corp., 882 F.2d 881, 883 (4th Cir. 1989)) (internal quotation marks omitted).

226. Express Freight Lines, Inc. v. Kelly (*In re* Express Freight Lines, Inc.), 130 B.R. 288, 290 (Bankr. E.D. Wis. 1991); Elsinore Shore Assocs. v. First Fid. Bank, N.A. (*In re* Elsinore Shore Assocs.), 67 B.R. 926, 942 (Bankr. D.N.J. 1986).

227. WATERMAN, *supra* note 221, at 9.

228. *See* Styler v. Jean Bob Inc. (*In re* Concept Clubs, Inc.), 154 B.R. 581, 586–87 (D. Utah 1993).

229. *See id.*

Regardless of the flavor, a creditor benefits from setoff because its claim is elevated from unsecured to secured status.[230] Instead of receiving a dividend from the estate in discounted bankruptcy dollars, the creditor's claim will be paid in full to the extent the estate owes money to the creditor.[231] Because the right of setoff is derived from state law, it arguably does not stem from the bankruptcy itself.[232]

A setoff's categorization within or without the claims allowance process is more difficult as a split of authority has developed over the issue. Led by *Commercial Financial Services, Inc. v. Jones* (*In re Commercial Financial Services, Inc.*), some courts have found that a setoff invokes the claims allowance process. When invoked by a creditor, setoff requires a valid enforceable debt against the estate.[233] This is true regardless of whether setoff is employed as an affirmative defense or counterclaim.[234] In contrast, *Styler v. Jean Bob Inc.* (*In re Concept Clubs, Inc.*) found the lack of necessity of a proof of claim controlling.[235] The filing of a proof of claim is not necessary to invoke the affirmative defense of setoff because it "only reduces, or extinguishes, the amount sought by the trustee for the estate."[236] Because the creditor need not file a proof of claim to assert the affirmative defense of setoff, *In re Concept Clubs* found that the claims allowance process was not implicated.[237]

Recent cases have found *In re Commercial Financial Services* more persuasive, and considering this Article's earlier analysis of reclama-

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230. *See* 11 U.S.C.A. § 553 (West 2006).

231. Commercial Fin. Servs., Inc. v. Jones (*In re* Commercial Fin. Servs., Inc.), 251 B.R. 397, 405 (Bankr. N.D. Okla. 2000); *see also* United Structures of Am., Inc. v. G.R.G. Eng'g, S.E., 9 F.3d 996, 998–99 (1st Cir. 1993) (pursuant to setoff, "if Smith is in bankruptcy and Jones is permitted to reduce his $10,000 grain debt to Smith by $5,000 because of the unpaid cottage rental, Jones has (1) deprived the estate of $5,000 it would otherwise have had to benefit other creditors; and (2) received full value on his $5,000 claim against Smith, even though other creditors might not receive full value").

232. Ferriell, *supra* note 209, at 172–73; *see, e.g.*, *In re* Freeway Foods of Greensboro, Inc., 466 B.R. 750, 767 (Bankr. M.D.N.C. 2012) (citing Stern v. Marshall, 131 S. Ct. 2594, 2609 (2011)); *In re Commercial Fin. Servs., Inc.*, 251 B.R. at 403 (citing N. Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 80–86 (1982) (plurality opinion)).

233. *In re Commercial Fin. Servs., Inc.*, 251 B.R. at 406.

234. *Id.* at 406–07; *see also* Stoebner v. Leonard, O'Brien, Wilford, Spencer & Gale, Ltd. (*In re* O'Neill), Nos. 4-95-1477, 4-97-001, 1997 WL 615661, at *3 (Bankr. D. Minn. Oct. 2, 1997) (noting that a creditor who is entitled to set off the amount of its claims against the amount it owes to a debtor "has effectively received full payment on its claims instead of being limited to the amount of the Trustee's pro rata distribution").

235. Styler v. Jean Bob Inc. (*In re* Concept Clubs, Inc.), 154 B.R. 581, 586–87 (D. Utah 1993).

236. *Id.* at 589.

237. *Id.*

tion, as well as *Stern's* analysis, the reliance is well placed.[238] The direct impact of the claimed setoff on the distribution of the debtor's assets, either as an affirmative defense or a counterclaim, implicates the claims allowance process.[239] The creditor must have an enforceable claim against the bankruptcy estate to offset his debt.[240] Moreover, as noted earlier, *Katchen* commented that a counterclaim by the estate, even for damages exceeding the proof of claim, does not fall outside of the claims allowance process due to its affirmative nature.[241] As illustrated by the analysis of reclamation, a proof of claim is not necessary for a party to engage in the claims allowance process.[242] Therefore, regardless of the flavor of setoff, it implicates the claims allowance process, and a bankruptcy court may enter a final judgment on the setoff and any estate counterclaims necessarily resolved by the setoff.[243] Lastly, a debtor's use of state-law setoff rights, as distinguished from a creditor's employment of § 553, requires the application of the *Stern* test as a state-law-based counterclaim by the estate cannot be finally adjudicated by the bankruptcy court unless it is necessarily resolved by the claims allowance process.[244] Because a setoff by definition arises from unrelated transactions, satisfaction of the second prong of *Stern* is unlikely.[245]

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238. *See, e.g.*, Hedstrom Corp. v. Wal-Mart Stores, Inc. (*In re* Hedstrom Corp.), No. 04-38543, 2006 WL 1120572, at *3 (N.D. Ill. Apr. 24, 2006); Crum v. Blixseth (*In re* Big Springs Realty LLC), 430 B.R. 629, 636 (Bankr. D. Mont. 2010); Elec. Mach. Enters. v. Hunt Constr. Grp. (*In re* Elec. Mach. Enters.), 416 B.R. 801, 871 (Bankr. M.D. Fla. 2009).

239. *See In re Hedstrom Corp.*, 2006 WL 1120572, at *3. However, one should not completely rely upon *Hedstrom's* analysis of *In re Commercial Financial Services*. *Hedstrom* held that any "setoff" which had "any effect on the assets of the bankruptcy estate must be adjudicated by a bankruptcy court." Paloian v. Geneva Seal, Inc. (*In re* Canopy Fin., Inc.), 471 B.R. 218, 221 (N.D. Ill. 2012). As noted by *In re Canopy Financial*, the *In re Commercial Financial Services* court extended its holding too far by abandoning the focus on the defendant possessing a valid, enforceable debt owed by the estate. *Id.*

240. Commercial Fin. Servs., Inc. v. Jones (*In re* Commercial Fin. Servs., Inc.), 251 B.R. 397, 407 (Bankr. N.D. Okla. 2000).

241. Katchen v. Landy, 382 U.S. 323, 337–38 (1966); *see* Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 60 n.14 (1989) (explaining *Katchen's* quote that "it makes no difference, so far as petitioner's Seventh Amendment claim is concerned, whether the bankruptcy trustee urges only a § 57g objection or also seeks affirmative relief").

242. *See supra* Part IV(C)(2).

243. *See* Columbia Hosp. for Women Med. Ctr., Inc. v. NCRIC, Inc. (*In re* Columbia Hosp. for Women Med. Ctr., Inc.), 461 B.R. 648, 657 (Bankr. D.D.C. 2011). Prior to *Katchen*, at least one circuit court did not allow a bankruptcy court to summarily offset a director's proof of claim against a permissive counterclaim. Dwyer v. Franklin (*In re* Majestic Radio & Television Corp.), 227 F.2d 152, 156 (7th Cir. 1955). However, the Seventh Circuit's analysis is unpersuasive because it relied upon the consent rationale rather than the claims allowance process used by *Katchen*. *Id.*

244. Somerset Props. SPE LLC v. LNR Partners, Inc. (*In re* Somerset Props. SPE, LLC), No. 10-09210-8-SWH, 2012 WL 3877791, at *8 (Bankr. E.D.N.C. Sept. 6, 2012).

245. *Id.* at *8–9.

4. Recoupment[246]

In contrast to setoff, recoupment is the diminishment of the debtor's claim against a defendant resulting from the defendant invoking a defense, which arises from the same transaction that underlies the debtor's claim.[247] Recoupment, unlike setoff, is a creature of the common law.[248] It is distinguished from setoff because it is "confined to matters arising out of, and connected with, the transaction or contract upon which the suit is brought."[249] An express contractual right to recoupment is not necessary;[250] a defendant can recoup damages from a tort against a claim of the estate from a contract.[251] Recoupment is available in one flavor, an affirmative defense, and any excess balance cannot be recovered.[252] Because recoupment is derived from the common law and is not governed by the Code, it is uncertain whether it stems from the bankruptcy itself.[253] Then-Circuit Judge Breyer explained that codification is unnecessary "because a debtor has, in a sense, no right to funds subject to recoupment."[254] If available, recoupment has significant advantages compared to setoff.[255] Because § 553 does not govern recoupment, its requirement that the

246. This analysis assumes that the defendant seeking recoupment has also not filed a proof of claim. If a proof of claim had been filed, the usual claims allowance process inquiry is required and the bankruptcy court may adjudicate the recoupment defense if it would be resolved by the claims allowance process. *See* Sundale, Ltd. v. Fla. Assocs. Capital Enters., No. 11-20635-CIV, 2012 WL 488110, at *5–6 (S.D. Fla. Feb. 14, 2012), *aff'd*, No. 12-11450, 2012 WL 5974125, at *4 (11th Cir. Nov. 29, 2012).

247. For other hypotheticals explaining the differences between the two doctrines see, for example, United Structures of Am., Inc. v. G.R.G. Eng'g, S.E., 9 F.3d 996, 998–99 (1st Cir. 1993), and John T. Seybert, *Recoupment in the Health Care Industry–Is it Equitable?*, 6 AM. BANKR. INST. L. REV. 495 (1998). *See also* Ashland Petrol. Co. v. Appel (*In re* B & L Oil Co.), 782 F.2d 155, 157–58 (10th Cir. 1986) (canvassing various examples drawn from prior cases).

248. WATERMAN, *supra* note 221, at 466.

249. ALEXANDER R. TIFFANY, A TREATISE ON THE POWERS AND DUTIES OF JUSTICES OF THE PEACE IN THE STATE OF MICHIGAN 277 n.1 (The Richmond & Backus Co. eds., 8th ed. 1886).

250. Holford v. Powers (*In re* Holford), 896 F.2d 176, 179 (5th Cir. 1990); *In re B & L Oil Co.*, 782 F.2d at 159.

251. WATERMAN, *supra* note 221, at 423, 444–45.

252. Rothensies v. Elec. Storage Battery Co., 329 U.S. 296, 299 (1946); Bull v. United States, 295 U.S. 247, 262 (1935); *see also* WATERMAN, *supra* note 221, at 466.

253. However, bankruptcy courts have so far found that they have Constitutional Power to decide what constitutes the property of the estate as stemming from the bankruptcy itself. *See infra* Part V(B)(4).

254. United Structures of Am., Inc. v. G.R.G. Eng'g, S.E., 9 F.3d 996, 999 (1st Cir. 1993).

255. Theoretically, the two doctrines should be mutually exclusive as either two actions are sufficiently related to allow recoupment or they are unrelated and setoff could potentially be used; however, courts may stretch the definition of related or unrelated to allow either of the doctrines to apply. *See* 1 DAVID G. EPSTEIN ET AL., BANKRUPTCY 703 (1992) (describing the liberal interpretation of "related" applied in *In re B & L Oil Co.*).

debt arise prepetition is not applicable.[256] Hence, the defense of recoupment may arise post-petition.[257] As a reduction of the debtor's estate to determine its correct value, instead of a transfer, recoupment is not subject to avoidance as a preferential transfer.[258] Additionally, "[t]he trustee . . . takes the property subject to rights of recoupment," and therefore, recoupment is not restrained by the automatic stay.[259] A typical example of recoupment would involve a creditor who failed to pay for a shipment of wheat from the debtor after the wheat became wet due to negligence of the debtor.[260] The creditor could recoup the money spent drying out the wheat from the debt he owed the estate for failure to pay for the shipment.[261]

On the spectrum spanning from counterclaims that invoke the claims allowance process to defenses that do not, recoupment sits at the midpoint between the ends. Unsurprisingly, courts are split over whether recoupment is part of the claims allowance process.[262] Some courts view recoupment, which can only be raised defensively, as a defense apart from the claims allowance process while others consider the mitigation of payment to the estate as a distribution invoking the claims allowance process.[263] A number of courts have found that recoupment should not be deemed to provide a distribution from the estate even if the amount the trustee recovers is reduced.[264] Instead, recoupment "ascertain[s] the true value of the estate" by justly reduc-

256. *See generally* 11 U.S.C.A. § 553 (West 2006).

257. *See, e.g.*, Ashland Petrol. Co. v. Appel (*In re* B & L Oil Co.), 782 F.2d 155, 156, 158 (10th Cir. 1986) (noting that the post-petition debts of the defendant could be recouped).

258. *E.g.*, *In re* Yonkers Hamilton Sanitarium Inc., 22 B.R. 427, 433 (Bankr. S.D.N.Y. 1982), *aff'd sub. nom.* Sapir v. Blue Cross/Blue Shield of Greater N.Y. (*In re* Yonkers Hamilton Sanitarium Inc.), 34 B.R. 385 (S.D.N.Y. 1983).

259. Holford v. Powers (*In re* Holford), 896 F.2d 176, 179 (5th Cir. 1990) (quoting Brock v. Career Consultants, Inc. (*In re* Career Consultants, Inc.), 84 B.R. 419, 426 (Bankr. E.D. Va. 1988)) (internal quotation marks omitted).

260. *E.g.*, United Structures of Am., Inc. v. G.R.G. Eng'g, S.E., 9 F.3d 996, 998–99 (1st Cir. 1993). For other examples, see Seybert, *supra* note 247, at 495, and *In re B & L Oil Co.*, 782 F.2d at 157–58, for an overview of examples drawn from prior cases.

261. *United Structures of Am., Inc.*, 9 F.3d at 999.

262. *Compare* Paloian v. Geneva Seal, Inc. (*In re* Canopy Fin., Inc.), 471 B.R. 218, 223 (N.D. Ill. 2012) (explaining that because a defendant's affirmative defense has nothing to do with a claim against the debtor's estate, it is not part of the claims allowance process), *and* Container Recycling Alliance v. Lassman, 359 B.R. 358, 365 (D. Mass. 2007) (asserting a fair accounting of the estate is not part of the claims allowance process), *with* Scott v. Santander Consumer, USA, Inc. (*In re* Scott), No. 12-50388, 2012 WL 3952973, at *2 (Bankr. W.D. Tex. Sept. 10, 2012) (noting that recoupment claims are part of the claims allowance process).

263. *In re Canopy Fin., Inc.*, 471 B.R. at 223; *Lassman*, 359 B.R. at 365.

264. *See generally In re Canopy Fin., Inc.*, 471 B.R. 218; *Lassman*, 359 B.R. 358.

ing the estate's recovery on the transaction as a whole.[265] This view characterizes recoupment as "essentially a defense."[266] Thus, the estate "takes the property subject to the rights of recoupment," and "the debtor has no interest in the funds" subject to those rights.[267] A defense to an estate's claim that, if successful, would diminish the estate's property should not invoke the claims allowance process.[268] In contrast, one bankruptcy court has recently found that recoupment is "part and parcel of the claims allowance process."[269] It relied upon an opinion of the Fifth Circuit, which characterized recoupment as similar to setoff because it "operates as an exception to the rule that all unsecured creditors of a bankrupt stand on equal footing for satisfaction [and] . . . sometimes allows particular creditors preference over others."[270]

The better view is that a creditor's action for recoupment does not invoke the claims allowance process. While mutual debts are required to apply a setoff, a defense, like recoupment, directly alters the amount sought by the plaintiff. It must be conceded that recoupment reduces the total value of the estate.[271] Yet, its focus on determining the just and proper liability owed to the estate on the basis of the estate's claim, instead of obtaining a distribution from the estate, tips the scales in favor of characterizing it as a defense and against it invoking the claims allowance process.[272] Hence, it is better viewed as a defense to the estate's claim, and it does not invoke the claims allowance process. Additionally, a claim by the estate for recoupment would fit within a bankruptcy court's Constitutional Power only if it was necessarily resolved in the claims allowance process.[273]

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265. *Lassman*, 359 B.R. at 364; *see In re Canopy Fin., Inc.*, 471 B.R. at 222; Riley v. Wolverine, Proctor & Schwartz, Ltd. (*In re* Wolverine, Proctor & Schwartz, LLC), 404 B.R. 1, 4 (D. Mass. 2009).

266. Lee v. Schweiker, 739 F.2d 870, 875 (3d Cir. 1984).

267. Holford v. Powers (*In re* Holford), 896 F.2d 176, 179 (5th Cir. 1990).

268. *Lassman*, 359 B.R. at 364. *But see* Somerset Props. SPE LLC v. LNR Partners, Inc. (*In re* Somerset Props. SPE, LLC), No. 10-09210-8-SWH, 2012 WL 3877791, at *9 (Bankr. E.D.N.C. Sept. 6, 2012).

269. Scott v. Santander Consumer, USA, Inc. (*In re* Scott), No. 12-50388, 2012 WL 3952973, at *2 (Bankr. W.D. Tex. Sept. 10, 2012).

270. U.S. Abatement Corp. v. Mobil Exploration & Producing U.S., Inc. (*In re* U.S. Abatement Corp.), 79 F.3d 393, 398 (5th Cir. 1996).

271. *Lassman*, 359 B.R. at 364.

272. United Structures of Am., Inc. v. G.R.G. Eng'g, S.E., 9 F.3d 996, 998–99 (1st Cir. 1993) (citations omitted); *Lassman*, 359 B.R. at 364–65; *cf.* Crist, *supra* note 13, at 671–72.

273. *Id.* (citing *In re Somerset Props. SPE, LLC*, 2012 WL 3877791, at *8).

5. Administrative Expenses

When analyzing whether the claims allowance process applies to administrative expenses, two issues have split courts. First, whether administrative expenses invoke the claims allowance process at all; and second, whether § 502(d) applies to administrative expenses in the same way it does to § 501(a) claims. Additionally, due to its unique character, § 503(b)(9) warrants a separate analysis of the applicability of § 502(d). In contradistinction to the § 502 claims allowance process outlined earlier in this Part, administrative expense requests are governed by § 503, which sets forth the procedure for their allowance; a proof of claim is explicitly unnecessary.[274] "Thus, with respect to the allowance of claims, sections 502 and 503 are separate and independent."[275] The majority of courts addressing this issue have agreed with the Second Circuit and found that § 503(b) requests are not claims within the meaning of § 501(a), the usual avenue for invoking the claims allowance process.[276] Nevertheless, the claims allowance process should be invoked by a request for administrative expenses pursuant to § 503(b).[277] Whether § 502(d) should be applied to administrative expenses is more uncertain.

Although post-*Stern* no published opinion has analyzed whether § 503(b) is part of the claims allowance process, pre-*Stern* courts were split over whether a request for administrative expenses invoked the claims allowance process. Most courts found that administrative expenses should not be distinguished from § 501 claims[278] because they "are still claims against the debtor's estate and hence seek a piece of the res."[279]

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274. *E.g.*, ASM Capital, LP v. Ames Dep't Stores, Inc. (*In re* Ames Dep't Stores, Inc.), 582 F.3d 422, 429 n.4 (2d Cir. 2009) (per curiam) (noting that the official proof of claim form cautions that it should not be used to file for an administrative expense claim which is governed by § 503).

275. *Id.* at 430.

276. *In re* Circuit City Stores, Inc., 426 B.R. 560, 569 (Bankr. E.D. Va. 2010) (noting the majority rule and listing cases).

277. *Cf. In re Ames Dep't Stores, Inc.*, 582 F.3d at 429 n.5 ("But doing business with the reorganized debtor and filing a request for payment of administrative expenses might have other consequences, such as waiving the vendor's right to a jury trial in any preference action initiated by the debtor.").

278. *E.g.*, Billing v. Ravin, Greenberg & Zackin, P.A., 22 F.3d 1242, 1253 (3d Cir. 1994); Roberds, Inc. v. Palliser Furniture, 291 B.R. 102, 107 (S.D. Ohio 2003); Cibro Petrol. Prods., Inc. v. City of Albany (*In re* Winimo Realty Corp.), 270 B.R. 108, 122 (S.D.N.Y. 2001); O'Neill v. New England Rd., Inc., No. 3:99MC 309 SRU, 2000 WL 435507, at *7 (D. Conn. Feb. 28, 2000); Simmons v. Johnson, Curney & Fields, P.C. (*In re* Simmons), 205 B.R. 834, 850 (Bankr. W.D. Tex. 1997).

279. *O'Neill*, 2000 WL 435507, at *7.

In contrast, the Western District of North Carolina held that the allowance of administrative expenses was not part of the claims allowance process.[280] After the defendant accounting firm sought allowance of their fees as an administrative expense, the trustee counterclaimed for breach of contract, negligent misrepresentation, and fraud in regard to the prepetition services.[281] The defendants sought a jury trial.[282] Although the court admitted that the broadest definition of claim would encompass administrative expense requests, they were "not the sort of claims contemplated by the Code" as invoking the claims allowance process.[283] The court clarified that "the Code goes further and narrows the meaning of a claim and segregates professional 'claims' out, designating them as expenses."[284] Accordingly, the fee request was not part of the claims allowance process.[285]

A number of reasons strongly suggest administrative expense requests are part of the claims allowance process. Most importantly, the Code defines claims as a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured."[286] The breadth of this definition is not accidental as "Congress gave the broadest possible definition to the term 'claim' in order to ensure that all legal obligations of the debtor . . . [would] be dealt with in the bankruptcy case."[287] This definition is sufficiently broad to include administrative expenses, and the claims allowance process has not been expressly limited to § 501 claims.[288] Moreover,

280. Bowers v. McGladrey & Pullen (*In re* Fla. Hotel Props. LP), 163 B.R. 757, 759 (W.D.N.C. 1994).

281. *Id.* at 758.

282. *Id.* Although the divergence between the post-petition expenses and the prepetition actions would not have satisfied the *Stern* test due to the lack of a complete overlap, the district court did not apply that analysis. Nonetheless, at least one court has generously cited *In re Florida Hotel Properties* for the proposition that "the filing of an administrative claim does not waive a right of jury trial when a party demands a jury trial in an *unrelated proceeding*." Lu v. Grant (*In re* Sunshine Trading & Transp. Co.), 193 B.R. 752, 755 (Bankr. E.D. Va. 1995) (emphasis added) (citing *In re Fla. Hotel Props. LP*, 163 B.R. 757).

283. *In re Fla. Hotel Props. LP*, 163 B.R. at 759.

284. *Id.*

285. *See id.*; *cf.* Billing v. Ravin, Greenberg & Zackin, P.A., 22 F.3d 1242, 1259 (3d Cir. 1994) (Sloviter, C.J., dissenting) (noting that "there is some question whether the attorneys' claim for fees is comparable to a creditor's pre-petition claim"). Interestingly, *In re Florida Hotel Properties* noted that defendants may have submitted to the "administrative jurisdiction of the Bankruptcy Court" when they request allowance of their fees. *In re Fla. Hotel Props. LP*, 163 B.R. at 759.

286. 11 U.S.C. § 101(5)(A) (2006).

287. Sigmon v. Royal Cake Co. (*In re* Cybermech, Inc.), 13 F.3d 818, 821 (4th Cir. 1994) (citations omitted) (internal quotation marks omitted).

288. *E.g.*, *In re* Momenta, Inc., 455 B.R. 353, 361 (Bankr. D.N.H. 2011).

"'claims' and 'expenses' are not mutually exclusive labels as several provisions in the Bankruptcy Code include administrative expenses within the claims label."[289] The analysis of setoff as an affirmative defense also teaches that a proof of claim is not necessary for an entity to invoke the claims allowance process. The requirements and process for allowance of administrative expenses under § 503(b) is analogous to the process used to allow claims using § 502 or the process of reclamation under § 546(c).[290] Each adjudicates whether a claimant receives a "piece of the bankruptcy estate."[291] A request for allowance of administrative expenses invokes the claims allowance process.

This Part previously detailed the impact of § 502(d) on the claims allowance process. Whether administrative expense requests are governed by the restrictions of § 502(d) is a separate issue that presents a triple split of authority. The majority view holds that § 502(d) is not applicable to any § 503 requests for administrative expenses.[292] The minority view espouses the opposite view,[293] while *In re Circuit City Stores* applied § 502(d) to only § 503(b)(9).[294] The minority position relies upon the inclusion of administrative expenses within the scope of § 57(g) of the 1898 Act and the Code's retention of the same scope in § 502(d). In *Weber v. Mickelson* (*In re Colonial Services Co.*), the Eighth Circuit found that an administrative expense was governed by § 57(g) and that the expense claim would not be allowed until a preference was surrendered.[295] The court's ruling relied upon two sources. It found that the plain language of § 57(g)—"[t]he claims of creditors who have received or acquired preferences . . . void or avoidable under this title, shall not be allowed unless such creditors shall surrender such preferences"—required surrender of a voidable preference by an administrative expense claimant.[296] In delineating the scope to § 57(g), *In re Colonial Services* also relied upon *Irving Trust*

289. *Id.*

290. *Cf.* Peachtree Lane Assocs. v. Granader, 175 B.R. 232, 237 (N.D. Ill. 1994) ("Resolution of post-petition claims as with many—albeit not all—other administrative expenses are as much a function of the bankruptcy court's equitable apportionment of the estate as resolution of pre-petition claims.").

291. *E.g.*, *id.*; Simmons v. Johnson, Curney & Fields, P.C. (*In re* Simmons), 205 B.R. 834, 850 (Bankr. W.D. Tex. 1997) (noting that the "defendants participated in the process of allowance and disallowance of claims by seeking and accepting payments of fees and claiming a share of the estate as a priority creditor").

292. *In re Momenta, Inc.*, 455 B.R. at 361 (listing cases).

293. *E.g.*, MicroAge, Inc. v. Viewsonic Corp. (*In re* MicroAge, Inc.), 291 B.R. 503 (B.A.P. 9th Cir. 2002); *see also* Movitz v. Baker (*In re* Triple Star Welding, Inc.), 324 B.R. 778, 794 (B.A.P. 9th Cir. 2005) (applying *In re MicroAge*).

294. *In re* Circuit City Stores, Inc., 426 B.R. 560, 571 (Bankr. E.D. Va. 2010).

295. 480 F.2d 747, 749 (8th Cir. 1973).

296. *Id.* at 749 (quoting § 57(g) of the 1898 Act).

Co. v. Frimitt, which found that administrative expense claimants were among the claimants vulnerable to § 57(g) objections.[297] Later courts adopting the minority position have relied upon the legislative history of § 502(d). Section 502(d) was "derived from the present law,"[298] meaning § 57(g) of the 1898 Act. Without expressed intent to change the pre-Code practice of applying § 57(g) to administrative expenses, proponents of the minority view argue that the same parameters, as outlined by *In re Colonial Services*, should apply under the Code.[299]

In *ASM Capital, LP v. Ames Department Stores, Inc.* (*In re Ames Department Stores, Inc.*), the Second Circuit disagreed with *In re Colonial Services* and adopted the majority position, holding that § 502(d) was not applicable to § 503(b) administrative expenses.[300] *In re Ames Department Stores* examined how § 501 claims are compartmentalized from § 503(b) administrative expense requests with different procedures for filing and allowance.[301] Moreover, the language of § 502(d) strongly suggests that it applies solely to those claims that are otherwise allowable; it only applies "[n]otwithstanding subsections (a) and (b) of this section."[302] Section 503(b) is a mandatory provision without exceptions: an expense that satisfies § 503(b) shall be allowed. Unlike the quoted language making subsections (a) and (b) of § 502 subject to § 502(d), § 503 is not listed. Hence, the application of § 502(d) to § 503(b) creates an unnecessary conflict between two mandatory subsections.[303] *In re Ames Department Stores* also found *In re Colonial Services* to be "weak authority."[304] The plain language of the statute changed with the Code, and the application of § 57(g) in *Irving Trust Co.* may not have even been disputed.[305]

Although *In re Circuit City Stores* applied § 502(d) to only § 503(b)(9),[306] its analysis was persuasively rejected by *In re Mo-*

297. Irving Trust Co. v. Frimitt, 1 F. Supp. 16, 17 (S.D.N.Y. 1932).

298. *In re MicroAge, Inc.*, 291 B.R. at 508–09 (quoting H.R. REP. No. 95-595, at 354 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6310) (internal quotation marks omitted); S. REP. No. 95-989, at 65 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5851, 5963, 6309–10.

299. *In re MicroAge, Inc.*, 291 B.R. at 509.

300. 582 F.3d 422 (2d Cir. 2009) (per curiam).

301. *Id.* at 429–30.

302. *Id.* at 430.

303. *Id.* at 430–31.

304. *Id.* at 431 n.6.

305. *In re Ames Dep't Stores, Inc.*, 582 F.3d at 422, 431 n.6.

306. Section 503(b)(9) allows an administrative expense for "the value of any goods received by the debtor within 20 days before the date of commencement of a case under this title in which the goods have been sold to the debtor in the ordinary course of such debtor's business." 11 U.S.C. § 503(b)(9) (2006). This recently enacted paragraph of the Code has proven extremely troublesome. *See, e.g.*, Brendan M. Gage, Note, *Should Congress Repeal Bankruptcy Code Section 503(B)(9)?*, 19 AM. BANKR. INST. L. REV. 215 (2011); Nick Sears, Comment, *Defeating the*

menta.[307] *In re Circuit City Stores* required the filing of a proof of claim for § 503(b)(9) expense requests.[308] It characterized § 503(b)(9) as unique among § 503(b) administrative expenses; a proof of claim would be required for a claimant to receive a distribution because a § 503(b)(9) request relates to prepetition goods received by the debtor in the twenty days prior to the petition date.[309] Because a proof of claim is required pursuant to § 501(a), § 502 in general, and subsection (d) in particular, applied to the § 503(b)(9) request for expenses.[310] *In re Momenta* disagreed by finding that a § 501(a) proof of claim was not required. Although a claimant could file a proof of claim under § 501(a), a request for administrative expenses does not require the filing of a proof of claim and the employment of § 502.[311]

The application of the claims allowance process to administrative expenses in general and the effect, if any, of § 502(d), are unsettled. The better argument, as explained above, fits administrative expenses within the claims allowance process. Determining the effect of § 502(d) is more difficult. Both the minority and majority positions have compelling arguments with further policy implications beyond the claims allowance process.[312] Although a circuit court, especially the Eighth Circuit, could reasonably rely upon *In re Colonial Services* instead of *In re Ames Department Stores*, *In re Ames Department Stores's* argument is reasonable and, as a much more recent opinion, it is more persuasive.

6. Informal Proofs of Claim[313]

Informal claims are claims which lack the proper form under Bankruptcy Rule 3001[314] but contain sufficient substance to be deemed a proof of claim by a bankruptcy court.[315] The modern test[316] for infor-

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Preference System: Using the Subsequent New Value Defense and Administrative Expense Claims to "Double Dip", 28 EMORY BANKR. DEV. J. 593 (2012).

307. *In re* Momenta, Inc., 455 B.R. 353 (Bankr. D.N.H. 2011).

308. *In re* Circuit City Stores, Inc., 426 B.R. 560, 570 (Bankr. E.D. Va. 2010).

309. *Id.* at 569–70 ("If a 'creditor' wishes to be granted an administrative priority under § 503(b)(9), then the creditor must, first, file a proof of claim under § 501, second, have the claim allowed under § 502, and then, third, request administrative expense priority under § 503(a).").

310. *Id.* at 569.

311. *In re Momenta, Inc.*, 455 B.R. at 364.

312. *See* Paul R. Hage, *Does § 502(d) Apply to Administrative Expenses?—The Second Circuit Joins the Debate in In re Ames Department Stores*, 18 J. BANKR. L. & PRAC. 6, 4 (2009).

313. Because Leslie Masterson recently chronicled many applications of the informal claims to the claims allowance process, this Article will attempt to cover other issues untouched by her article. *See* Masterson, *supra* note 43, at 113–14, 120–22.

314. FED. R. BANKR. P. 3001.

315. Masterson, *supra* note 43, at 98.

mal proofs of claim is a five-part test formulated by the Tenth Circuit in *Clark v. Valley Federal Savings & Loan Ass'n* (*In re Reliance Equities, Inc.*).[317] It requires that:

1. the proof of claim must be in writing;
2. the writing must contain a demand by the creditor on the debtor's estate;
3. the writing must express an intent to hold the debtor liable for the debt;
4. the proof of claim must be filed with the Bankruptcy Court; and
5. based on the facts of the case, it would be equitable to allow the amendment.[318]

Most courts have equated the filing of a counterclaim against the estate seeking damages, an informal proof of claim, with the filing of a proof of claim for purposes of invoking the claims allowance process.[319] In contrast, *Busch–Provo, Ltd. v. Sloan* (*In re Larsen*) limited this principle by reasoning that the claims allowance process could not be triggered by an informal proof of claim.[320] This limitation has been roundly criticized by subsequent opinions.[321] One better reasoned exception allows an informal claimant to elude the claims allowance process when his counterclaim cannot be adjudicated by the bankruptcy court.[322] For instance, an informal proof of claim for a personal injury tort or a wrongful death claim must be tried in a district court.[323]

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316. For a summary of the historical origins of the informal claim doctrine, see *id.* at 97–98.

317. 966 F.2d 1338 (10th Cir. 1992); *see, e.g.*, Hefta v. Official Comm. of Unsecured Creditors (*In re* Am. Classic Voyages Co.), 405 F.3d 127, 131 (3d Cir. 2005) (adopting the five-part test); Barlow v. M.J. Waterman & Assocs., Inc. (*In re* M.J. Waterman & Assocs., Inc.), 227 F.3d 604, 609 (6th Cir. 2000) (same); Nikoloutsos v. Nikoloutsos (*In re* Nikoloutsos), 199 F.3d 233, 236 (5th Cir. 2000) (adopting the Tenth Circuit's test).

318. *In re Reliance Equities, Inc.*, 966 F.2d at 1345.

319. *See, e.g.*, Leshin v. Welt (*In re* Warmus), 276 B.R. 688, 693 (S.D. Fla. 2002); Murray v. Richmond Steel & Welding Co. (*In re* Hudson), 170 B.R. 868, 874 (E.D.N.C. 1994); Peachtree Lane Assocs., Ltd. v. Granader, 175 B.R. 232, 236–37 (N.D. Ill. 1994); Segal v. Cal. Energy Dev. Corp., 167 B.R. 667, 672 (D. Utah 1994); Altman v. Alt. Debt Portfolios, L.P. (*In re* EZ Pay Servs., Inc.), 389 B.R. 278, 287 (Bankr. M.D. Fla. 2008); Schwinn Plan Comm. v. AFS Cycle & Co. Ltd. (*In re* Schwinn Bicycle Co.), 184 B.R. 945, 953 (Bankr. N.D. Ill. 1995).

320. 172 B.R. 988, 993 (D. Utah 1993).

321. *See, e.g.*, *Granader*, 175 B.R. at 236 n.6; Rushton v. Phila. Forest Prods., Inc. (*In re* Americana Expressways, Inc.), 161 B.R. 707, 712 n.9 (D. Utah 1993); Condrey v. Endeavour Highrise, L.P. (*In re* Endeavour Highrise L.P.), 425 B.R. 402, 411–13 (Bankr. S.D. Tex. 2010) (listing cases criticizing *Larsen* and agreeing with critiques).

322. *See* Control Ctr., LLC v. Lauer, 288 B.R. 269, 286 (M.D. Fla. 2002).

323. 28 U.S.C. § 157(b)(5) (2006); *Lauer*, 288 B.R. at 286; *see* Germain v. Conn. Nat'l Bank, 988 F.2d 1323, 1327 (2d Cir. 1993) ("28 U.S.C. § 157(b)(5) requires bankruptcy litigants to try any personal injury or wrongful death action in the district court. This strongly suggests that these litigants are entitled to a jury trial in such an action even after a proof of claim has been filed in bankruptcy court.").

When analyzing informal proofs of claim, the limitations of the *Stern* test apply. Many of the pre-*Stern* cases failed to analyze whether the informal claim would be completely resolved in the claims allowance process of adjudicating the informal proof of claim.[324] *Stern's* requirement of the necessary resolution of all legal and factual issues as part of ruling on the informal proof of claim will often preclude a bankruptcy court's Constitutional Power over an estate's counterclaim because the necessary overlap will not exist.[325] When applicable, § 502(d) should apply to ease this requirement.[326]

The Sixth Circuit recently applied the claims allowance process to an informal proof of claim in *Waldman v. Stone* without specifically identifying the creditor's counterclaim as an informal proof of claim.[327] *Waldman* exhibited an unusual procedural posture. The debtor-in-possession brought a number of common-law actions against a creditor who had not filed a proof of claim.[328] The creditor responded by filing a counterclaim seeking a judgment on his prepetition claim in lieu of filing a proof of claim.[329] The creditor's counterclaim sought a distribution from the bankruptcy estate and therefore triggered the claims allowance process.[330] The actions of the debtor-in-possession, which would be necessarily resolved in ruling on the creditor's counterclaim, were within the bankruptcy court's Constitutional Power.[331] However, the debtor-in-possession's claims presenting factual or legal issues that would not be necessarily resolved by ruling on the creditor's counterclaim were not within the bankruptcy court's Constitutional Power.[332]

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324. This view is known as the conversion theory. *See* Masterson, *supra* note 43, at 116 n.202, 116–17 (explaining the conversion theory and listing cases).

325. Shipley Garcia Enters., LLC v. Cureton, No. M-12-89, 2012 WL 3249544, at *10 (S.D. Tex. Aug. 7, 2012); *see* Stern v. Marshall, 131 S. Ct. 2594, 2617 (2011).

326. *Cf. In re Americana Expressways, Inc.*, 161 B.R. at 712 n.9 (noting that a turnover action against a creditor who filed an informal proof of claim could be lodged as a counterclaim or as an objection pursuant to § 502(d)).

327. 698 F.3d 910 (6th Cir. 2012).

328. *Id.* at 920.

329. *Id.*

330. Brubaker, *Litigant Consent*, *supra* note 58, at 4–5; *see Waldman*, 698 F.3d at 920. The Court of Appeals distinguished a party who had not filed a proof of claim from a secured creditor who is not required to file a proof of claim to retain his right to recover from the estate. *Waldman*, 698 F.3d at 920. The import of this distinction is potentially troubling. Barring two exceptions, a secured creditor does not need to file a proof of claim to protect his interest during the pendency of a bankruptcy case. PCFS Fin. v. Spragin (*In re* Nowak), 586 F.3d 450, 455–56 (6th Cir. 2009). Why should a secured creditor, who has not filed a proof of claim and seeks his lien to emerge from bankruptcy unaffected, be categorized any differently than a third party who has not filed a proof of claim?

331. *Waldman*, 698 F.3d at 920–21.

332. *Id.* at 921.

7. Does the Claims Allowance Process Affect the Estate?

Usually, a creditor or stranger to the estate seeks to limit the bankruptcy court's Constitutional Power.[333] Nonetheless, the circuit courts are split over the rarer issue of how to apply the claims allowance process to the debtor or the estate. The *Stern* test in general, and the claims allowance process in particular, should apply equally to the debtor or the estate.

In *In re Jensen,* the Fifth Circuit extended the claims allowance process too far in holding that "[f]iling a proof of claim denied both the plaintiff and the defendant, the debtor, any right to jury trial that they otherwise might have had."[334] *Stern's* necessarily resolved test for the claims allowance process overrules this view as the filing of a proof of claim is not sufficient to satisfy its second prong. The filing of a proof of claim does not automatically grant Constitutional Power to a bankruptcy judge. Only if all of the issues presented in the action are resolved as part of the claims allowance do either of those consequences occur.

The Second Circuit allowed the estate to retain the right to a jury trial when its counterclaim would not be resolved in the process of ruling on the creditor's proof of claim.[335] In *Germain v. Connecticut National Bank*, the court applied a test similar to the *Stern* claims allowance process prong to allow an estate's right to a jury trial.[336] In *Germain*, the trustee retained his right to a jury trial because the trustee's claims were not resolved by adjudicating the defendant's proof of claim.[337] The court also rejected the analyses applied in *Jensen* by properly focusing on the overlap of the action with the claims allowance process.[338]

If an action is necessarily resolved as part of the claims allowance process, the bankruptcy court should be able to finally adjudicate it regardless of the consent of the debtor or the third party. *Stern* has

333. The belief that bankruptcy courts are debtor friendly and the resulting desire of adverse parties to have the district court adjudicate causes of action probably stems from "the historical fact that the referee's compensation was based wholly on a percentage of the amount disbursed to creditors as dividends; every claim on which the trustee prevailed was of direct financial benefit to the referee." Note, *supra* note 60, at 702 n.38; *see* M. Sobel, Inc. v. Weinstein (*In re* Weinstein), 237 B.R. 567, 574 (Bankr. E.D.N.Y. 1999); James Angell MacLachlan, *Protection and Collection of Property of Bankrupt Estates*, 39 MINN. L. REV. 626, 639 (1955).

334. 946 F.2d 369, 374 (5th Cir. 1991).

335. Germain v. Conn. Nat'l Bank, 988 F.2d 1323, 1330 (2d Cir. 1993).

336. *Id.* at 1329–30.

337. *Id.* Although *Germain* does not explicitly state the necessarily resolved portion of the *Stern* test, it did conclude that it "must be part of the claims-allowance process." *Id.* at 1330.

338. *Id.* at 1330. *See* Billing v. Ravin, Greenberg & Zackin, P.A., 22 F.3d 1242, 1251–52 (3d Cir. 1994) (coming to the same conclusion).

clarified that the action must be necessarily resolved by the claims allowance process, thereby torpedoing *In re Jensen*. Hence, the claims allowance process grants a bankruptcy court Constitutional Power over a common-law action—even if the estate does not consent—if the action will be necessarily adjudicated as part of the claims allowance process.[339] The same conclusion follows for the second prong of the *Stern* test analyzed in the next part. *Stern* did not limit the application of its test to third parties.[340] Part VI(B)(2) will also discuss why a debtor does not waive the right to Article III adjudication by filing a bankruptcy petition.[341] In the absence of limiting language in *Stern*, "[s]urely constitutionality does not turn on the alignment of the parties, that is, whether a common law cause of action is asserted by the estate against a third party or by a third party against the estate."[342]

V. STEMS FROM THE BANKRUPTCY ITSELF

Defining actions that stem from the bankruptcy itself is difficult as *Stern* failed to provide any examples.[343] However, by analyzing how Vickie Marshall's counterclaim did not fit within this prong, *Stern* limited the potential breadth of the prong. Providing limiting principles is important considering "virtually anything could be justified" as stemming from the bankruptcy itself.[344] Although *Stern* rejected Vickie's attempt to fit her claim within the public rights exception,[345] it left open the possibility for other portions of bankruptcy law to fit within the exception.[346] Additionally, *Stern* also approved of looking beneath a Code-based action to recharacterize it as a state-law or common-law claim requiring Article III adjudication.[347] This Part analyzes both the public rights exception and looking beneath an ac-

339. *See* Deitz v. Ford (*In re* Deitz), 469 B.R. 11, 27 n.3 (B.A.P. 9th Cir. 2012) (Markell, J., concurring).

340. Stern v. Marshall, 131 S. Ct. 2594, 2618 (2011).

341. *See infra* Part VI(B)(2).

342. L.T. Ruth Coal Co. v. Big Sandy Coal & Coke Co. (*In re* L.T. Ruth Coal Co.), 66 B.R. 753, 794 (Bankr. E.D. Ky. 1986).

343. At least one court has hinted that "stems from the bankruptcy itself" does not clothe bankruptcy courts with constitutional authority "to adjudicate disputes that closely resemble traditional private rights disputes." West v. Freedom Med., Inc. (*In re* Apex Long Term Acute Care–Katy, L.P.), 465 B.R. 452, 457 (Bankr. S.D. Tex. 2011).

344. *See* Lipson, *supra* note 29, at 612 (observing that anything could be considered part of the restructuring of debtor–creditor relations which has been rebranded by *Stern* as stemming from the bankruptcy itself).

345. *Stern*, 131 S. Ct. at 2618.

346. *Id.* at 2614 n.7.

347. Neither *Stern* nor *Marathon* required this analysis because they both involved state-law claims existing independent of the Code. *Id.* at 2615.

tion by considering how they were applied before *Stern*, in *Stern*, and after *Stern*.

A. *Public Rights Doctrine*

Although originally applied to disputes only between individuals and the government, the breadth of the public rights doctrine has grown to allow Congress greater power to grant non-Article III tribunals the power to adjudicate what would otherwise be actions requiring Article III adjudication.[348] Congress cannot "withdraw from judicial cognizance any matter which, from its nature, is the subject of a suit at the common law, or in equity, or admiralty."[349] The public rights exception to this rule represents the ability of Congress to entrust an Article I court with matters that would otherwise require Article III supervision, but for a waiver of sovereign immunity.[350] Much to Justice Scalia's annoyance, the public rights exception has expanded into "matters of private right, that is, of the liability of one individual to another under the law as defined."[351]

Justice O'Connor's majority opinions[352] in *Thomas v. Union Carbide Agricultural Products Co.*[353] and *Schor*[354] illustrate an expansive

348. *Id.* at 2620–21 (Scalia, J., concurring).

349. *Id.* at 2612 (citing Murray v. Hoboken Land & Improvement Co., 59 U.S. 272, 284 (1855)).

350. *Id.* (citing *Murray*, 59 U.S. at 283–84). The other two exceptions involve cases arising in the territories of the United States and the District of Columbia and military cases. *See* N. Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 64–66 (1982). Due to Congress's broad powers of governance over territories pursuant to Article IV of the Constitution, *see* Am. Ins. Co. v. Canter, 26 U.S. 511, 546 (1828) (Marshall, C.J.), Article III restrictions should not apply to bankruptcy courts located in territories outside of the mainland United States which are properly considered Article I courts. Glidden Co. v. Zdanok, 370 U.S. 530, 547 (1962) (listing cases). Hence, it is questionable whether the limits of the Constitutional Power of a bankruptcy court in the districts of Guam, the Virgin Islands, the Northern Mariana Islands, and Puerto Rico mirror those of the other bankruptcy courts. Interestingly, one of the first *Stern* cases occurred in the District of the Virgin Islands. *See* Springel v. Prosser (*In re* Innovative Commc'n Corp.), No. 07-30012, 2011 WL 3439291 (Bankr. D.V.I. Aug. 5, 2011).

351. *Stern*, 131 S. Ct. at 2612 (quoting Crowell v. Benson, 285 U.S. 22, 50, 51 (1932)) (internal quotation marks omitted) (noting the parameters of the public rights exception as quoted in *Crowell v. Benson*); *see id.* at 2620–21 (Scalia, J., concurring); Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 65–71 (1989) (Scalia, J., concurring).

352. The author doubts whether *Stern* would have been decided 5–4 against the constitutionality of 11 U.S.C. § 157(b)(2)(c) if Justice O'Connor were on the Court at the time the case was decided. Considering her opinions in *Thomas* and *Schor*, as well as her dissent in *Granfinanciera*, and her joining the majority in *Katz*, it seems probable she would have joined the four dissenters in upholding the constitutionality of 11 U.S.C. § 157(b)(2)(c). *See* Joseph Pace, *Bankruptcy as Constitutional Property: Using Statutory Entitlement Theory to Abrogate State Sovereign Immunity*, 119 YALE L.J. 1568, 1571–73 (2010).

353. 473 U.S. 568 (1985).

354. 478 U.S. 833 (1986).

public rights exception. The rise of the administrative agencies has led the Supreme Court to analyze the expertise of the decision maker as a factor in deciding whether the public rights exception applies.[355] For example, *Crowell v. Benson* lauded agency adjudication as a "prompt, continuous, expert, and inexpensive method."[356] This description could have been transplanted from an optimistic depiction of bankruptcy court proceedings.[357] In *Thomas*, the Court pronounced a vague test for private actions falling within the exception: "[Congress's] constitutional powers under Article I, may create a seemingly 'private' right that is so closely integrated into a public regulatory scheme . . . ."[358] This practical test weighed both the congressional intent and the benefits of Article I adjudication against the importance of Article III adjudication.[359] *Schor* affirmed the functional test used by *Thomas* and went even further to declare that the common-law character of a counterclaim against the CFTC was not dispositive in requiring Article III adjudication.[360] Although *Schor* admitted that the standard for finding the public rights exception applicable to a private common-law right is high, the "limited CFTC jurisdiction over a narrow class of common law claims as an incident to the CFTC's primary, and unchallenged, adjudicative function does not create a substantial threat to the separation of powers."[361] Following *Thomas* and *Schor*, the breadth and even vitality of *Marathon* was questioned.[362] Yet, in *Stern*, the Court followed the reasoning outlined in

355. Troy A. McKenzie, *Getting to the Core of* Stern v. Marshall*: History, Expertise, and the Separation of Powers*, 86 AM. BANKR. L.J. 23, 31 (2012). For a deep consideration of the Supreme Court's Article III jurisprudence in agency cases, see Thomas Merrill, *Article III, Agency Adjudication, and the Origins of the Appellate Review Model of Administrative Law*, 111 COLUM. L. REV. 939, 943–44 (2011).

356. 285 U.S. 22, 46 (1932).

357. *E.g.*, Bailey v. Glover, 88 U.S. 342, 346 (1874) ("It is obviously one of the purposes of the Bankrupt law, that there should be a speedy disposition of the bankrupt's assets. This is only second in importance to securing equality of distribution. The act is filled with provisions for quick and summary disposal of questions arising in the progress of the case, without regard to usual modes of trial attended by some necessary delay.").

358. *Thomas*, 473 U.S. at 593–94. Although at least one bankruptcy court has posited that the *Stern* test is an application of *Thomas's* imperative, West v. Freedom Med., Inc. (*In re* Apex Long Term Acute Care–Katy, L.P.), 465 B.R. 452, 460 (Bankr. S.D. Tex. 2011), one can easily distinguish *Thomas's* test because it notes that it applies to "agency resolution[s]." *Thomas*, 473 U.S. at 594.

359. Matson, *supra* note 79, at 503 (summarizing *Thomas*).

360. Commodity Futures Trading Comm'n v. Schor, 478 U.S. 833, 853 (1986).

361. *Id.* at 854.

362. Carl N. Pickerill, Note, *Specialized Adjudication in an Administrative Forum: Bridging the Gap Between Public and Private Law*, 82 NOTRE DAME L. REV. 1605, 1642 (2007) ("While *Schor* did not overrule *Northern Pipeline* explicitly, one must wonder whether *Northern Pipeline* still has staying power.").

Marathon and *Granfinanciera* by focusing on the independence of the cause of action from the Code and ruled that Vickie's counterclaim did not fall within the public rights exception.[363]

"Effectively, the federal government supplies the forum and standards for resolution of private debt matters" by a bankruptcy judge.[364] This description, together with the historical analysis of bankruptcy matters that is usually inapplicable in other public rights cases,[365] helps account for the limited impact of the public rights exception in bankruptcy cases. If the bankruptcy court were an "adjunct" to the district court,[366] or simply an administrative agency,[367] it could constitutionally adjudicate Vickie's counterclaim in *Stern*. Instead, Congress has attempted to make bankruptcy a matter of adjudication, not simply administration.[368] As Professor Baird recently highlighted, the question of agency jurisdiction is a modern issue, far post-dating *Murray's Lessee*.[369] Conversely, "the delegation of bankruptcy matters is historical" and draws upon the eighteenth century practices used in English courts.[370] Without the barriers of historical restrictions on adjudication, the adjudicative powers of modern government agencies are more likely to fall within the public rights exception.[371] These two distinctions help explain how the counterclaim could be resolved by the CFTC in *Schor*, but the bankruptcy court in *Stern* could not resolve Vickie's counterclaim.[372]

Because the Supreme Court has been reluctant to analyze how the public rights framework is implicated by bankruptcy itself,[373] it is impossible to prove that a particular action fits within it. Bankruptcy

363. McKenzie, *supra* note 355, at 32 n.39 (listing *Stern's* repeated iterations of this point).

364. Susan M. Freeman & Marvin C. Ruth, *The Scope of Bankruptcy Ancillary Jurisdiction After* Katz *as Informed by Pre-*Katz *Ancillary Jurisdiction Cases*, 15 AM. BANKR. INST. L. REV. 155, 155 (2007).

365. *See* Baird, *supra* note 12, at 15.

366. Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 158–59 (discussing the adjunct theory and the difficulties of applying it to bankruptcy courts).

367. Professor Baird poses an interesting counterfactual analysis of the bankruptcy court as an administrative agency. Baird, *supra* note 12, at 15.

368. Lipson, *supra* note 29, at 654.

369. Baird, *supra* note 12, at 15.

370. *Id.*

371. *Id.*

372. *Id.*; *see also supra* Part II(B) (discussing distinctions between the CFTC and bankruptcy courts with regards to consent).

373. Stern v. Marshall, 131 S. Ct. 2594, 2614 n.7 (2011) (citing and quoting *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33, 56 n.11 (1989)); Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 172 (asserting that *Stern* maintained "maximum flexibility should it ever choose to revisit the constitutionality of bankruptcy judges' adjudicatory authority. . . . [S]ome of the potential constitutional justifications that the Court analyzed (such as the public rights doctrine as applied to bankruptcy adjudications) likely will not stand.").

courts have relied upon *Thomas's* "closely integrated" test to find that certain elements of the Code are part of the public rights exception.[374] However, the lack of evidence for what portions of the Code, if any, fit within the public rights exception makes any reliance on the "closely integrated" test more conjecture than analysis.[375] At least one bankruptcy court has recently expressed skepticism over whether the public rights exception should be applied to bankruptcy at all, considering both the Supreme Court's failure to employ the exception in *Stern* or *Granfinanciera* and the inherent difficulties of compartmentalizing the exception.[376]

B. *Looking Beneath the Action*

Recharacterizing Code-based actions as common-law issues[377] limits the Constitutional Power of bankruptcy courts.[378] Yet, *Stern* explicitly approved of the Seventh Amendment Case Line's use of this technique to decipher whether an action seeks either "a pro rata share

374. *E.g.*, Farooqi v. Carroll (*In re* Carroll), 464 B.R. 293, 312 (Bankr. N.D. Tex. 2011); Kirschner v. Agoglia (*In re* Refco Inc.), 461 B.R. 181, 191 (Bankr. S.D.N.Y. 2011). For the most complete analysis of the public rights exception's potential application to bankruptcy, see West v. Freedom Med., Inc. (*In re* Apex Long Term Acute Care–Katy, L.P.), 465 B.R. 452, 457–60 (Bankr. S.D. Tex. 2011).

375. *Stern*, 131 S. Ct. at 2615 (describing the exception as "amorphous"); *see In re* Clay, 35 F.3d 190, 194 (5th Cir. 1994) ("The public rights/private rights dichotomy of *Crowell* and *Murray* is a deceptively weak decisional tool."); Burtch v. Huston (*In re* USDigital, Inc.), 461 B.R. 276, 290 n.79 (Bankr. D. Del. 2011) ("[T]he constitutional validity of the heart of the bankruptcy courts' decision-making authority has not been resolved.").

376. Moyer v. Koloseik (*In re* Sutton), 470 B.R. 462, 469–73 (Bankr. W.D. Mich. 2012).

377. Although both *Stern* and *Marathon* concerned state-law-based actions, a bankruptcy court should also be forbidden from finally adjudicating a federal contract-law-based action. Humboldt Express, Inc. v. Wise Co. (*In re* Apex Express Corp.), 190 F.3d 624, 633 (4th Cir. 1999) ("We believe, however, that the federal nature of the dispute involved is only incidental to the question being discussed. . . . A pre-petition state-based contract claim and a pre-petition federal-based contract claim stand in the same position vis-a-vis the statutory language of § 157(b)(2) and vis-a-vis the core public rights function of bankruptcy courts."). *In re Apex Express* highlights a significant problem with relying on pre-*Stern* precedent. Prior to *Stern*, courts did not believe that a core but precluded category existed. *See In re Refco Inc.*, 461 B.R. at 186. Instead many courts analyzed core proceedings in light of *Marathon*, and any case that came too close to *Marathon's* prohibition was noncore, i.e. not core but precluded. Hence, many cases that might have been more properly adjudicated as core but precluded were simply found to be noncore. Matson, *supra* note 79, at 484–85, 491 (discussing the drawbacks of finding accounts receivable actions as noncore even when they should be considered turnover proceedings which are core). Interestingly, a somewhat similar situation occurred when *Katchen* abandoned the consent framework employed by lower courts. *Cf.* Rochelle & King, *supra* note 62, at 681–96 (discussing the circuit court's consent-focused analysis, which became outmoded after *Katchen*).

378. *See* Joyner v. Liprie (*In re* Liprie), No. 10-21281, 2012 WL 1144614, at *3 (Bankr. W.D. La. Apr. 4, 2012).

of the bankruptcy res" or "to augment the bankruptcy estate."[379] Reconciling the pragmatic view that *Stern* did not represent a seismic shift in bankruptcy courts' Constitutional Power with *Stern's* approval of this technique is difficult. Below, this Article analyzes different applications of looking beneath the action.

1. Involuntary Taking Subject to Fifth Amendment Protection

First in *Meoli v. Huntington National Bank (In re Teleservices Group)*,[380] and as later expounded by *Moyer v. Koloseik (In re Sutton)*,[381] Judge Hughes has adopted the most expansive view for looking beneath the action.[382] *In re Teleservices Group* and *In re Sutton* categorized those actions, which require the involuntary taking of property, as also requiring Article III adjudication unless the claims allowance process will necessarily adjudicate the action.[383] The court suggested returning to the roots of *Murray's Lessee* by conflating whether the opposing party has been deprived of the Fifth Amendment right to due process with whether an action does not stem from bankruptcy itself.[384] In other words, "if you want authorization to take someone else's property in the federal judicial system on account of an ordinary debt, you need to get it from an Article III judge."[385] Hence, a court should look beneath the action and consider, "Does this court have the constitutional authority to issue such an order on its own? Or does the Fifth Amendment's guaranty of due process require the oversight of an independent Article III judge before that order may enter?"[386] Although not stated directly by *In re Sutton*, if an action requires the involuntary taking of property, then the action cannot stem from the bankruptcy itself. Because each requires an involuntary taking of property, neither § 542 turnover actions[387] nor

379. *Stern*, 131 S. Ct. at 2618 (quoting Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 56 (1989)).

380. 456 B.R. 318 (Bankr. W.D. Mich. 2011).

381. 470 B.R. 462 (Bankr. W.D. Mich. 2012).

382. This view was later explained by Professor Douglas G. Baird, Baird, *supra* note 12, at 5, and both views were analyzed by Judge Bailey who found them persuasive. Murphy v. Felice (*In re* Felice), 480 B.R. 401, 413–15 (Bankr. D. Mass. 2012); *cf.* Tabor v. Kelly (*In re* Davis), No. 05-15794-GWE, 2011 WL 5429095, at *13 (Bankr. W.D. Tenn. Oct. 5, 2011) (also positively citing Judge Hughes's analysis in *In re Teleservices Group*).

383. *In re Sutton*, 470 B.R. at 472.

384. *Id.* at 468; *In re Teleservices Grp.*, 456 B.R. at 329–33, 337 n.61.

385. Baird, *supra* note 12, at 5.

386. *In re Sutton*, 470 B.R. at 473. Put another way, "can [an entity] be deprived of [its] liberty, or property . . . without the exercise of the judicial power of the United States." *In re Teleservices Grp.*, 456 B.R. at 330 (quoting Murray v. Hoboken Land & Improvement Co., 59 U.S. 272, 275–76 (1855)).

387. *In re Sutton*, 470 B.R. at 473.

contested orders for relief in involuntary bankruptcy[388] stem from the bankruptcy itself.

In re Teleservices Group listed examples of actions that did not require Fifth Amendment due process protection, including a bankruptcy court's authorization of a trustee's power to sell estate property and its modification of the automatic stay.[389] The court explained that its ability to authorize the sale of property outside the ordinary course of a debtor's business stemmed from the ability of Congress to provide a trustee with the power to act in these situations without bankruptcy court approval.[390] Although the requirement of notice and a hearing is applicable, *In re Teleservices Group* asserts that the requirement is unnecessary because no taking of property occurred.[391] It "is only an administrative hurdle . . . to ensure that someone other than the trustee himself will consider the objections . . . and then decide whether the trustee should have authority to proceed notwithstanding."[392] Additionally, the imposition of or the subsequent modification to the automatic stay does not require a taking of property, even though it restricts access to Article III and state courts.[393] So far, Judge Hughes's and Professor Baird's views have not been widely espoused.[394] However, were their analyses to become more popular, it would further shake the landscape of bankruptcy courts' Constitutional Power.[395]

2. Fraudulent Transfers and Preferences

When analyzing the right to a jury trial, some courts have looked beneath Code-based causes of action to decide whether the right attached. The Ninth Circuit was the first circuit to follow *Stern's* reli-

388. *Id.* at 473 n.38; *In re Teleservices Grp.*, 456 B.R. at 333 n.50. Under an originalist interpretation of constitutional bankruptcy court jurisdiction, it is difficult to find a violation of due process created by an order for relief in an involuntary bankruptcy. The 1800 Act, enacted while many of the Framers were still in power, only allowed for an involuntary petition to be filed by creditors. *See* Kenneth N. Klee, *Legislative History of the New Bankruptcy Law*, 28 DEPAUL L. REV. 941, 941 n.1 (1979).

389. *In re Teleservices Grp.*, 456 B.R. at 333–34.

390. *Murray* also found that the "summary procedure used by the treasury . . . did not deprive [the defendant] of his right to due process." *Id.* at 330. The court used this same rationale to find that the court could adjudicate the allowance of claims. *Id.* at 336–37.

391. *Id.* at 334; *see also* Murphy v. Felice (*In re* Felice), 480 B.R. 401, 417–18 (Bankr. D. Mass. 2012).

392. *In re Teleservices Grp.*, 456 B.R. at 334.

393. *Id.* at 335.

394. According to Baird, the courts have long resisted applying the "logic of *Murray's Lessee*." Baird, *supra* note 12, at 12.

395. Lipson, *supra* note 29, at 612 ("[T]here is little question that bankruptcy's basic operations pass procedural muster.").

ance upon the Seventh Amendment Case Line and look beneath fraudulent transfers to characterize them as beyond the Constitutional Power of bankruptcy courts, unless they are necessarily resolved by ruling on a creditor's proof of claim. Starting with *Schoenthal*, the Supreme Court has expressly embraced this analysis.[396] There, the defendant of a § 60 preference action[397] retained the right to a jury trial.[398] Even though the 1898 Act codified § 60 preferences, they "constitute[d] no part of the proceedings in bankruptcy"[399] as preferences had long existed outside of bankruptcy.[400] *Katchen* subsequently reaffirmed *Schoenthal's* holding.[401] *Granfinanciera* equated a preference action with a fraudulent transfer and accordingly relied on *Schoenthal's* analysis to recharacterize a fraudulent transfer as a state-law-based counterclaim.[402] *Langenkamp* subsequently approved of the analysis in *Granfinanciera.*[403] *Stern* also approved of this analysis when it analogized Vickie's state-law-based counterclaim to the fraudulent conveyance in *Granfinanciera*, an action that is only state-law based when one looks beneath the codified action.[404] Many courts have followed the Seventh Amendment Case Line as precedent for recharacterizing §§ 544, 547, and 548 actions as state-law-based actions seeking to augment the bankruptcy estate, which require an Article III judge for final adjudication if they are not necessarily resolved by the claims allowance process.[405] Broader application to other sections of the Code has been sparse.[406]

In *In re Bellingham*, the Ninth Circuit recognized that "*Stern* fully equated bankruptcy litigants' Seventh Amendment right to a jury trial in federal bankruptcy proceedings with their right to proceed before

396. Schoenthal v. Irving Trust Co., 287 U.S. 92 (1932).

397. Now, such transfers would be categorized as § 547(b) preferences.

398. *Schoenthal*, 287 U.S. at 97.

399. *Id.* at 94–95.

400. *Id.* at 94 n.1.

401. Katchen v. Landy, 382 U.S. 323, 336 (1966).

402. *Schoenthal*, 287 U.S. at 94–95.

403. Langenkamp v. Culp, 498 U.S. 42, 45 (1990) (per curiam).

404. Stern v. Marshall, 131 S. Ct. 2594, 2614, 2618 (2011).

405. *E.g.*, Rosenberg v. Bookstein, No. 2:12-cv-00627-MMD-RJJ, 2012 U.S. Dist. LEXIS 135200, at *4 (D. Nev. Sept. 21, 2012); Weisfelner v. Blavatnik (*In re* Lyondell Chem. Co.), 467 B.R. 712, 721–22 (S.D.N.Y. 2012); Dev. Specialists, Inc. v. Akin Gump Strauss Hauer & Feld LLP, 462 B.R. 457, 468–69 (S.D.N.Y. 2011); Paloian v. Am. Express Co. (*In re* Canopy Fin., Inc.), 464 B.R. 770, 773 (N.D. Ill. 2011); Tucker v. Gibson (*In re* G & S Livestock Co.), No. 10-81378-FJO-7, 2012 Bankr. LEXIS 718, at *8 (Bankr. S.D. Ind. Sept. 5, 2012); Burns v. Dennis (*In re* Se. Materials, Inc.), 467 B.R. 337, 349–52 (Bankr. M.D.N.C. 2012).

406. At least two pre-*Stern* cases support this broader application. *See* DuVoisin v. Anderson (*In re* S. Indus. Banking Corp.), 66 B.R. 349, 356 (Bankr. E.D. Tenn. 1986); L.T. Ruth Coal Co. v. Big Sandy Coal & Coke Co. (*In re* L.T. Ruth Coal Co.), 66 B.R. 753, 792, 795–96 (Bankr. E.D. Ky. 1986).

an Article III judge."[407] As a result, the Seventh Amendment Case Line inhibits bankruptcy court final adjudication of either fraudulent transfers or preferences.[408] To find either type of action to constitute a public right would be "incoherent" considering the holdings of the Seventh Amendment Case Line.[409] Looking underneath an action to attack whether the action stems from the bankruptcy itself is not always successful. A growing number of courts have even refused to follow *Schoenthal*, *Granfinanciera*, and *Langenkamp* as precedent for looking underneath a fraudulent conveyance or preference.[410] They focus on the limiting language of *Stern* and refuse to graft *Schoenthal* and its progeny into the Constitutional Adjudication Case Line.[411] Considering *Stern's* reliance upon the Seventh Amendment Case Line, *In re Bellingham's* reliance upon it is natural and correct.

3. Post-Petition Transfers

Defendants have unsuccessfully tried to look beneath § 549 preference avoidance actions to reclassify them as actions existing outside of the Code. Courts have almost unanimously refused to look beneath § 549 post-petition transfer actions because they are vital to an orderly administration of a debtor's estate and are "essentially a creditor's remedy involving the equitable distribution of the bankrupt's estate."[412] Post-petition avoidance actions perform a different function

407. Exec. Benefits Ins. Agency v. Arkison (*In re* Bellingham Ins. Agency, Inc.), 702 F.3d 553, 563 (9th Cir. 2012).

408. *Id.* at 562–64. Although one can make a strong argument for distinguishing a fraudulent transfer from a preference for purposes of whether it stems from the bankruptcy itself, *see* West v. Freedom Med., Inc. (*In re* Apex Long Term Acute Care–Katy, L.P.), 465 B.R. 452, 462–64 (Bankr. S.D. Tex. 2011), the Supreme Court's conflation of the two in *Granfinanciera* weakens the argument.

409. *In re Bellingham Ins. Agency, Inc.*, 702 F.3d at 564.

410. *See, e.g.*, Monette v. United States (*In re* Custom Contractors, LLC), 462 B.R. 901, 908 (Bankr. S.D. Fla. 2011); Gugino v. Canyon Cnty. (*In re* Bujak), No. 10-03569, 2011 WL 5326038, at *3 (Bankr. D. Idaho Nov. 3, 2011); Heller Ehrman LLP v. Arnold & Porter, LLP (*In re* Heller Ehrman LLP), No. 08-32514DM, 2011 WL 4542512, at *6 (Bankr. N.D. Cal. Sept. 28, 2011); *In re* Safety Harbor Resort & Spa, 456 B.R. 703, 717 (Bankr. M.D. Fla. 2011).

411. *See, e.g.*, *In re Safety Harbor Resort & Spa*, 456 B.R. at 717 (explaining that the *Stern* court went to great lengths to limit the scope of its ruling).

412. Comm. of Unsecured Creditors of N.C. Hosp. Ass'n Trust Fund v. Mem'l Mission Med. Ctr., Inc. (*In re* N.C. Hosp. Ass'n Trust Fund), 112 B.R. 759, 762 (Bankr. E.D.N.C. 1990); *see* Parker v. Barkan & Robon Ltd. (*In re* Mackey), No. 09-30996, 2011 Bankr. LEXIS 3224, at *4 (Bankr. W.D. Ohio Aug. 22, 2011) (noting *In re N.C. Hospital Ass'n Trust Fund* represents the majority view). *Contra* Calaiaro v. Roberts (*In re* Roberts), 126 B.R. 678 (Bankr. W.D. Pa. 1991) (only case to look beneath a § 549 claim and hold that the right to a jury trial attaches). Post-*Stern*, one court also found that § 549 actions are within a bankruptcy court's Constitutional Power because they are "purely a creation of the Bankruptcy Code and [do] not otherwise exist outside of Title 11." Springel v. Prosser (*In re* Innovative Commc'n Corp.), No. 07-30012, 2011 WL 3439291, at *3 (Bankr. D.V.I. Aug. 5, 2011).

than fraudulent transfers. Section 549 actions safeguard the bankruptcy estate because "[t]he allowance and disallowance of claims becomes [sic] meaningless if the estate is decimated [by post-petition transfers] and there is nothing to distribute to creditors."[413] In further contrast to prepetition avoidance actions, they do not augment the estate and instead "restore property of the estate to the control of the bankruptcy court for proper administration."[414] Hence, they are far more likely to stem from the bankruptcy itself.

4. Estate Property

Courts have also resisted attempts to limit bankruptcy judges' Constitutional Power over determining what assets constitute property of a debtor's estate by recharacterizing the inquiry as a state-law issue.[415] The determination of what constitutes property of a debtor's estate is decided by state law.[416] Yet, bankruptcy courts have roundly found that the determination of what constitutes the property of a debtor's estate stems from the bankruptcy itself[417] because a "[c]ritical feature[ ] of every bankruptcy proceeding[,] . . . the exercise of exclusive jurisdiction over all of the debtor's property,"[418] would be stymied.[419] However, if a court were to follow the path of *Schoenthal* and consider whether an English bankruptcy commissioner in 1789 would have decided the contents of the estate, the court would find that the commissioner did not have the power to adjudicate what property was in the estate.[420] An English commissioner was clothed with the power "to deal only with that which is the bankrupt's estate; but [had] no power to determine what is the bankrupt's estate."[421] The courts of

413. *In re N.C. Hosp. Ass'n Trust Fund*, 112 B.R. at 762–63.

414. Murphy v. Felice (*In re* Felice), 480 B.R. 401, 428 (Bankr. D. Mass. 2012).

415. *E.g.*, Burns v. Dennis (*In re* Se. Materials, Inc.), 467 B.R. 337, 452–53 (Bankr. M.D.N.C. 2012) ("There can be no dispute that this Court has the authority to determine what is and is not property of the Debtor's bankruptcy estate and enter final orders regarding the same."); *In re* Washington Mutual, Inc., 461 B.R. 200, 217 (Bankr. D. Del. 2011); Crist, *supra* note 13, at 669 & n.244.

416. Butner v. United States, 440 U.S. 48, 54–56 (1979).

417. *See, e.g.*, Olivie Dev. Grp. v. Park, No. C11-1691Z, 2012 WL 1536207, at *4 (W.D. Wash. Apr. 30, 2012); Velo Holdings Inc. v. Paymentech, LLC (*In re* Velo Holdings Inc.), 475 B.R. 367, 384 (Bankr. S.D.N.Y. 2012); BankUnited Fin. Corp. v. FDIC (*In re* BankUnited Fin. Corp.), 462 B.R. 885, 893–94 (Bankr. S.D. Fla. 2011).

418. Cent. Va. Cmty. Coll. v. Katz, 546 U.S. 356, 364 (2006); Tenn. Student Assistance Corp. v. Hood, 541 U.S. 440, 447 (2004) ("[T]he [bankruptcy] court's jurisdiction is premised on the debtor and his estate . . . .").

419. *See In re Velo Holdings Inc.*, 475 B.R. at 385 (determining that the estate's property is an "essential part of administration of the bankruptcy estate").

420. Halford v. Gillow, 60 Eng. Rep. 18, 20 (Ch. 1842) (discussing eighteenth century English bankruptcy jurisdiction); McCoid, *supra* note 21, at 29–31.

421. *Halford*, 60 Eng. Rep. at 20.

Westminster, both in law and equity, decided the contents of the bankrupt's estate.[422] Looking beneath the codified ability of a bankruptcy court to decide the composition of the estate would significantly curtail bankruptcy courts' Constitutional Power.[423] Although it seems likely that determining the contents of the estate would stem from the bankruptcy itself, at least one commentator has suggested that when state-law-based rights are adjudicated as part of determining the bankruptcy estate, an Article III judge is necessary.[424]

C. *Dependency and but for Causation*

Does a bankruptcy court have Constitutional Power over an action that would never have arisen without the bankruptcy case but is not created by federal bankruptcy law? Do actions arise from the bankruptcy itself because they are created by the Code, even though they are derived from state law? These issues were created by slightly loose wording in *Stern*. When distinguishing between Vickie's state-law-based counterclaim and the preference actions in *Katchen* and *Langenkamp*, the Court reasoned that the preference actions represented "a right of recovery created by federal bankruptcy law."[425] Vickie's claim, in contrast, is in no way derived from or dependent upon bankruptcy law; it is a state-law action that exists without regard to any bankruptcy proceeding."[426] However, *Stern* made clear that a proceeding that has "*some* bearing on a bankruptcy case" is not sufficient to stem from the bankruptcy itself.[427] Thus, at least two issues surrounding but for causation remain: (1) whether an action derived from or depended upon a bankruptcy proceeding, but not created by the Code, stems from the bankruptcy itself and (2) whether an action created by bankruptcy law automatically stems from the bankruptcy itself.

When confronted with the first issue in *Ortiz v. Aurora Health Care, Inc.* (*In re Ortiz*), the Seventh Circuit found that even if the existence of an action directly resulted from the bankruptcy proceeding, a bankruptcy court could not finally adjudicate it if it was created by nonbankruptcy law.[428] In *In re Ortiz*, the creditor, Aurora Health Care, Inc. (Aurora), filed proofs of claim in many bankruptcy cases from 2003 to

422. McCoid, *supra* note 21, at 29–31.
423. Plank, *supra* note 22, at 615.
424. Ferriell, *supra* note 209, at 175.
425. Stern v. Marshall, 131 S. Ct. 2594, 2599 (2011).
426. *Id.* at 2618.
427. *Id.*
428. Ortiz v. Aurora Health Care, Inc. (*In re* Ortiz), 665 F.3d 906, 914 (7th Cir. 2011).

2008, listing the debtors' medical information.[429] Many of the debtors participated in two class action suits against Aurora based upon a Wisconsin statute creating a cause of action for the disclosure of medical records without permission.[430] The court noted that the actions were within the core statutory jurisdiction of the Code by "arising in bankruptcy"[431] because they "would have no existence outside of the bankruptcy."[432] However, the court found the *Stern* test unsatisfied. All the factual and legal issues presented by the debtors' counterclaims would not be adjudicated in the process of resolving Aurora's proofs of claim.[433] Moreover, the debtors' counterclaims "owe[d] [their] existence to Wisconsin state law."[434] Therefore, even though the bankruptcy was the "but for" cause of the debtors' counterclaims, they did not stem from the bankruptcy itself.[435]

In a situation paralleling *Ortiz*, the Bankruptcy Court for the District of Delaware found that state-law claims, which arise out of actions taken in the bankruptcy case, stem from the bankruptcy itself.[436] In *In re American Business I* and *II*, the Chapter 7 trustee sued the debtor-in-possession lender for breach of fiduciary duty, breach of contract, and other state-law and bankruptcy-law causes of action.[437] The court found that regardless of the state-law basis of many of the actions, they would not exist but for the bankruptcy case.[438] The actions stemmed from the bankruptcy itself because they "relate[d] entirely to matters integral to the bankruptcy case."[439]

Proceedings involving § 544(b) present the second issue because it is dependent upon the bankruptcy law, even though it is derived from state law. The dependency of § 544(b) upon the Code is strong because it "may only be prosecuted by a bankruptcy trustee on behalf of

429. *Id.* at 908.

430. *Id.* (citing WIS. STAT. § 146.84 (2011)).

431. *See* 28 U.S.C. § 157(b)(1) (2006).

432. *In re Ortiz*, 665 F.3d at 911 (quoting Stoe v. Flaherty, 436 F.3d 209, 216 (3d Cir. 2006)) (internal quotation marks omitted).

433. *Id.* at 914.

434. *Id.*

435. *Id.*

436. Miller v. Greenwich Capital Fin. Prods., Inc. (*In re* Am. Bus. Fin. Servs., Inc. II), 471 B.R. 354, 362 (Bankr. D. Del. 2012).

437. *Id.* at 361–62; Miller v. Greenwich Capital Fin. Prods., Inc. (*In re* Am. Bus. Fin. Servs., Inc. I), 457 B.R. 314, 319–20 (Bankr. D. Del. 2012).

438. *In re Am. Bus. Fin. Servs., Inc. I*, 457 B.R. at 319–20 ("If not for the bankruptcy, these claims would never exist.").

439. *In re Am. Bus. Fin. Servs., Inc. II*, 471 B.R. at 361–62; *In re Am. Bus. Fin. Servs., Inc. I*, 457 B.R. at 319–20.

a bankruptcy estate."[440] "[B]ecause a trustee and a bankruptcy estate are strictly creatures of the Bankruptcy Code, there would be no legal basis for this action were there no bankruptcy case."[441] The trustee's position transforms § 544(b) from an action by a creditor under state law to provide personal benefit into an action by a representative of the bankruptcy estate for the benefit of all creditors.[442] However, § 544(b) requires employment of the applicable state law.[443] Once again, the key analysis is whether the Seventh Amendment Case Line, including *Granfinanciera*, is precedent for the right of a bankruptcy court to adjudicate an action. *Granfinanciera* is precedent for a § 548 action failing to stem from the bankruptcy itself even though it has no direct link to state law besides its historical roots.[444] Consequently, a § 544 action, with less dependence on the Code, does not stem from the bankruptcy itself.[445]

This conundrum of proceedings dependent upon the Code but incorporating state law also arises for § 365 executory contract disputes.[446] On the one hand, the power to assume or reject an unexpired lease is unique to the Code. On the other hand, a lease may not be assumed unless it is unexpired, a state-law-based issue.[447] Courts have relied upon the dependency of the action on the Code, as well as the link to the bankruptcy court's ability to determine the property of the estate,[448] as reasons that the determination of whether a debtor may assume an executory contract stems from the bankruptcy itself.[449] The ties to determining the estate's property and its reliance on the Code for existence increase the likelihood that § 365 actions stem from the bankruptcy itself. However, the reliance on

440. Gugino v. Canyon Cnty. (*In re* Bujak), No. 10-03569-JDP, 2011 WL 5326038, at *2 (Bankr. D. Idaho Nov. 3, 2011).

441. *Id.* at *2.

442. *Id.* at *3. This is the crux of bankruptcy's *raison d'être*, solving the common pool problem. *See* Thomas H. Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditor's Bargain*, 91 YALE L.J. 857, 861–62 (1982).

443. Silverman v. A–Z RX LLC (*In re* Allou Distribs. Inc.), No. 8-03-82321-ess, 2012 WL 6012149, at *10 (Bankr. E.D.N.Y. Dec. 3, 2012).

444. Adelphia Recovery Trust v. FLP Grp., No. 11 Civ. 6847 (PAC), 2012 U.S. Dist. LEXIS 10804, at *8–9 (S.D.N.Y. Jan. 30, 2012).

445. *See id.* at *9.

446. Ferriell, *supra* note 209, at 162–65.

447. *E.g.*, City of Valdez v. Waterkist Corp. (*In re* Waterkist Corp.), 775 F.2d 1089, 1091 (9th Cir. 1985).

448. Velo Holdings Inc. v. Paymentech, LLC (*In re* Velo Holdings Inc.), 475 B.R. 367, 387 (Bankr. S.D.N.Y. 2012) (property of the estate); Bustamante v. J. Moss Invs., Inc. (*In re* J. Moss Invs., Inc.), No. 12-50105, 2012 WL 2150346, at *3–4 (Bankr. S.D. Tex. June 12, 2012) (unique nature).

449. *In re Velo Holdings Inc.*, 475 B.R. at 387.

state law as the rule of decision prior to the application of the Code creates uncertainty.[450] For instance, in *L.T. Ruth Coal Co., Inc. v. Big Sandy Coal & Coke Co. (In re L.T. Ruth Coal Co., Inc.)*,[451] a well-reasoned bankruptcy court opinion closely following the enactment of BAFJA, the court would have held that it could not constitutionally adjudicate a debtor's assumption of leases due to the necessity of applying the underlying state law, if that option had not been foreclosed by a previous district court ruling.[452]

D. *Turnover Proceedings*

Although bona fide turnover proceedings should stem from the bankruptcy itself, distinguishing such proceedings from contractual disputes is often difficult as the line between property rights and contract rights is blurry.[453] A bona fide turnover action is not an action to augment the estate; it is an action to recover property of the estate.[454] Section 542 was added to the Code to solidify the turnover power of bankruptcy courts.[455] It had hitherto been a judicial creation.[456] Without the power to require turnover, administration of estate property could be hindered by uncooperative parties possessing estate property.[457] They "essentially are proceedings that would not exist outside of bankruptcy,"[458] and looking beneath them will not reveal a state-law-based action. In *Maggio v. Zeitz*, the Supreme Court supported this conclusion when it noted the similarity between turnover and the ancient actions of detinue and replevin, but it did not equate them because "the modern remedy does not exactly follow any of these ancient and often overlapping procedures."[459] *Maggio* also rejected that turnover is analogous to actions for trover or conversion.[460] Relying on the Supreme Court's analysis, the First Circuit

450. L.T. Ruth Coal Co. v. Big Sandy Coal & Coke Co. (*In re* L.T. Ruth Coal Co.), 66 B.R. 753, 782 (Bankr. E.D. Ky. 1986).

451. *Id.*

452. *Id.* 795–96.

453. Ferriell, *supra* note 209, at 146. This argument presupposes Judge Hughes's Fifth Amendment analysis does not apply. *See supra* Part V(B)(1).

454. Braunstein v. McCabe, 571 F.3d 108, 122 (1st Cir. 2009).

455. United States v. Whiting Pools, Inc., 674 F.2d 144, 156 (2d Cir. 1982), *aff'd*, 462 U.S. 198 (1983).

456. Maggio v. Zeitz, 333 U.S. 56, 62–63 (1948).

457. Fulton Cnty. Silk Mills v. Irving Trust Co. (*In re* Lilyknit Silk Underwear Co.), 73 F.2d 52, 54 (2d Cir. 1934). This rationale mirrors the reasons § 549 actions stem from the bankruptcy itself. *See Braunstein*, 571 F.3d at 123.

458. *See* Montana v. Goldin (*In re* Pegasus Gold Corp.), 394 F.3d 1189, 1193 (9th Cir. 2005); Burns v. Dennis (*In re* Se. Materials, Inc.), 467 B.R. 337, 357 (Bankr. M.D.N.C. 2012).

459. *Maggio*, 333 U.S. at 63.

460. *Id.*

looked beneath a turnover action and found that it should not be recharacterized as a common-law action for trover or conversion.[461] Following *Stern*, courts have held that bankruptcy courts possess Constitutional Power over bona fide turnover proceedings because they allow the gathering and managing of the estate's property and thus stem from the bankruptcy itself.[462]

Distinguishing bona fide turnover actions from contractual disputes is imperative when considering whether any turnover actions should stem from the bankruptcy itself. The differing breadths of § 542 and 28 U.S.C. § 157(b)(2)(E) create a category of bona fide turnover actions that a bankruptcy court may finally adjudicate and a category consisting of state-law-based disputes that an Article III tribunal must finally adjudicate.[463] If the debtor is owed debts that are "matured, payable on demand or payable on order" or a party other than the trustee has the possession, custody, or control of property of the estate, then § 542 requires turnover to the estate's representative.[464] However, 28 U.S.C. § 157(b)(2)(E) allows a bankruptcy court to issue final orders requiring turnover of estate property as a core proceeding. Pursuant to § 541, estate property includes a debtor's right to an account receivable or other disputed contract claim.[465] Disputed contract claims and accounts receivable actions naturally fit within the definition of turnover used by 28 U.S.C. § 157(b)(2)(E).[466] However, *Marathon* is direct precedent that a bankruptcy court cannot finally adjudicate a state-law-based contract dispute.[467] Hence, if a bankruptcy court has core jurisdiction over a disputed contract-based turn-

461. *Braunstein*, 571 F.3d at 121–22.

462. *See In re* Hernandez, 468 B.R. 396, 400 n.4 (Bankr. S.D. Cal. 2012); *In re Se. Materials, Inc.*, 467 B.R. at 357; Rentas v. Claudio (*In re* Garcia), 471 B.R. 324, 330 (Bankr. D.P.R. 2012). At least one court has mistakenly found that turnover's power to ensure "proper constitution of the estate" satisfies the claims allowance process prong of *Stern*. *In re Garcia*, 471 B.R. at 330.

463. Ferriell, *supra* note 209, at 144–46.

464. 11 U.S.C. § 542 (2006).

465. *Id.* § 541(a); Ferriell, *supra* note 209, at 146. Some courts have held that this category of claims is not a turnover claim within the core jurisdiction bestowed by 28 U.S.C. § 157(b)(2)(E). *See* Charter Crude Oil Co. v. Exxon Co. (*In re* Charter Co.), 913 F.2d 1575, 1579 (11th Cir. 1990); Dev. Specialists, Inc. v. Peabody Energy Corp. (*In re* Coudert Bros.), No. 11 Civ. 4949(PAE), 2011 WL 7678683, at *4 (S.D.N.Y. Nov. 23, 2011) (listing cases). As previously stated, if an action is not core, it is not subject to the *Stern* test. *See supra* notes 107–11 and accompanying text.

466. Ferriell, *supra* note 209, at 145; *see* Lovald v. Falzerano (*In re* Falzerano), 686 F.3d 885, 887 n.2 (8th Cir. 2012) (suggesting unjust enrichment determination as part of a § 542 final adjudication was potentially problematic under *Stern*).

467. *In re Charter Co.*, 913 F.2d at 1579; Dayton Title Agency, Inc. v. Phila. Indem. Ins. Co. (*In re* Dayton Title Agency, Inc.), 264 B.R. 880, 883–84 (Bankr. S.D. Ohio 2000); Ferriell, *supra* note 209, at 145–46; *cf. In re Falzerano*, 686 F.3d at 887 n.2 ("The bankruptcy court resolved the merits of the Trustee's unjust enrichment claim under state law, without identifying any tangible

over claim,[468] it may fit within the ambit of the core but precluded proceedings. Drawing the line between a contract dispute masquerading as a turnover proceeding has always been difficult.[469]

The dividing line used by the 1898 Act should not be resurrected to help decide which turnover actions bankruptcy courts may finally adjudicate. Under the 1898 Act, a turnover proceeding could be summarily adjudicated when the court possessed constructive possession because a defendant lacked a substantial defense to the turnover action.[470] A plenary proceeding was required when a defendant possessed a colorable defense.[471] The dividing line between a lack of a substantial defense and a colorable defense was very fact specific and difficult to predict.[472] Hence, it bred large amounts of litigation.[473] Professor Ferriell convincingly criticized a reversion to 1898 Act standards on the grounds that "those restraints were not at all based upon notions of what was permissible by the separation of powers doctrine," and instead focused on federalism.[474] A turnover action stems from the bankruptcy itself when the state law necessary to determine the turnover simply returns property to the estate instead of augmenting the estate. Actions pursuant to § 542 retrieve property of the estate or concern uncontested debts and do not augment the estate like some core turnover actions.[475] As a result, § 542 claims should stem from the bankruptcy itself.[476]

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property of the bankruptcy estate at issue other than the alleged debt. This would require further analysis to be upheld under *Stern*.").

468. This issue is also uncertain. *Compare* Burns v. Dennis (*In re* Se. Materials, Inc.), 467 B.R. 337, 355–56 (Bankr. M.D.N.C. 2012), *with* Humboldt Express, Inc. v. Wise Co., Inc. (*In re* Apex Express Corp.), 190 F.3d 624, 631–32 (4th Cir. 1999).

469. *See* Ferriell, *supra* note 209, at 145–46 ("Absent a means for distinguishing between state contract actions of the type involved in *Northern Pipeline* and traditional turnover proceedings, it is doubtful whether bankruptcy courts should be able to enter final judgments in turnover proceedings brought pursuant to section 542 of the Bankruptcy Code.").

470. May v. Henderson, 268 U.S. 111, 115–16 (1925); Brubaker, *Federal Bankruptcy Jurisdiction*, *supra* note 42, at 792; *see* Taubel-Scott-Kitzmiller Co. v. Fox, 264 U.S. 426, 432–33 (1924) (listing ways a trustee can have constructive possession).

471. *May*, 268 U.S. at 115–16; Harris Trust & Sav. Bank v. Keig (*In re* Prima Co.), 98 F.2d 952, 957 (7th Cir. 1938); Brubaker, *Federal Bankruptcy Jurisdiction*, *supra* note 42, at 792.

472. Brubaker, *Federal Bankruptcy Jurisdiction*, *supra* note 42, at 792–93, 793 n.177.

473. *Id. at* 792 (describing it as a "minitrial"); *cf. In re* Eddy, 279 F. 919, 920 (W.D.N.Y. 1922) ("There must be inquiry into the merits of such a controversy. It cannot here be determined on opposing affidavits.").

474. Ferriell, *supra* note 209, at 146.

475. *See* Rentas v. Claudio (*In re* Garcia), 471 B.R. 324, 328–30 (Bankr. D.P.R. 2012).

476. When a creditor has filed a proof of claim and the trustee asserts a turnover action, § 502(d), as outlined above, requires the adjudication of the turnover action prior to ruling on the creditor's proof of claim. 11 U.S.C. § 502(d) (2006). Hence, turnover is sometimes necessarily resolved as part of the claims allowance process. *See* Burns v. Dennis (*In re* Se. Materials, Inc.), 467 B.R. 337, 356, 357 n.29 (Bankr. M.D.N.C. 2012).

VI. DISCHARGEABILITY AND LIQUIDATION

Nondischargeability is an excellent place to end an analysis of the two prongs of *Stern* because it involves (1) the claims allowance process, (2) what stems from the bankruptcy itself, (3) whether to look underneath a claim, (4) jury trial and summary/plenary issues, and (5) even a hint of the intersection of *Stern* and subject matter jurisdiction. Moreover, it also "straddles" the line between administration of the estate and the application of judicial power.[477] The determination of nondischargeability stems from the bankruptcy itself. However, nondischargeability proceedings often involve the more constitutionally suspect liquidation of the debt.[478] Courts have erroneously relied upon pre-*Stern* cases analyzing whether the liquidation of a nondischargeable debt is core. Instead, courts should analyze Seventh Amendment cases construing the right to a jury trial for liquidation. Recently, a bankruptcy court has broken ranks in finding that liquidation of a nondischargeable debt does not stem from the bankruptcy itself.[479] Guided by *Stern* and Seventh Amendment cases, courts should employ the dischargeability allowance process. The dischargeability allowance process allows liquidation of a nondischargeable debt within a bankruptcy court's Constitutional Power when the factual and legal issues presented by the liquidation of the nondischargeable debt are fully determined as part of the nondischargeability proceeding.

A. *Dischargeability*

If anything truly stems from the bankruptcy itself, it is a debtor's discharge. As both Professors Countryman and Tabb explain, discharge in England prior to the founding, and in the United States from the 1800 Act onwards, has always been a statutory remedy with limitations and exceptions set by the sovereign.[480] The classes of individuals who could receive a discharge, the actions or omissions that could deny a debtor a discharge, as well as the types of debts excepted

477. Baird, *supra* note 12, at 4–5.

478. Dragisic v. Boricich (*In re* Boricich), 464 B.R. 335, 336–37 (Bankr. N.D. Ill. 2011). When a creditor has already obtained a prepetition judgment, which serves as the basis for the nondischargeability claim, the bankruptcy court need not reliquidate the debt. *See* Morrison v. W. Builders of Amarillo, Inc. (*In re* Morrison), 555 F.3d 473, 479 n.3 (5th Cir. 2009).

479. Johnson v. Weihert (*In re* Weihert), No. 12-10893, 2013 WL 485878, at *4 (Bankr. W.D. Wis. Feb. 6, 2013).

480. *See* Vern C. Countryman, *The New Dischargeability Law*, 45 AM. BANKR. L.J. 1 (1971); Charles Jordan Tabb, *The Historical Evolution of the Bankruptcy Discharge*, 65 AM. BANKR. L.J. 325 (1991) [hereinafter Tabb, *Evolution*].

from discharge, have all changed over the centuries,[481] but the standards across all three variables have always been set by the sovereign.[482] The increase in breadth of discharge from the original class of involuntary merchant debtors has never been tested in the Supreme Court.[483] However, while riding the circuit, Justice Catron relied upon the sovereign power over discharge to find constitutional the broadening of discharge to voluntary non-merchants under the 1841 Act.

> [Voluntary bankruptcy] was in violation of the leading principles on which English laws were founded. . . . But . . . [the Bankruptcy Clause] gives the unrestricted authority to congress over the entire subject, as the parliament of Great Britain had it, and as the sovereign states of this Union had it before the time when the constitution was adopted.[484]

Turning to the jury trial cases as precedent for the Article III issue, only one case, decided just after the advent of dischargeability, upheld a right to a jury trial on the issue of dischargeability.[485] Subsequently, courts have unanimously found that the right to a jury trial does not attach.[486] Neither in England at the time of the founding nor under any federal bankruptcy statute has the right to a jury trial on the subject of discharge or dischargeability been guaranteed.[487]

Following *Stern*, courts have unanimously found that determinations of dischargeability are within the Constitutional Power of bankruptcy courts.[488] In *Deitz v. Ford* (*In re Deitz*), the Bankruptcy Appellate Panel for the Ninth Circuit canvassed the post-*Stern* case

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481. The general trend has been towards a greater access to discharge with fewer acts causing a full denial. *See* Countryman, *supra* note 480; Tabb, *Evolution*, *supra* note 480. For instance, in England at the time of the founding in England and under the 1800 Act, only traders could receive a discharge. Tabb, *Evolution*, *supra* note 480, at 343, 346. Not until the 1841 Act was the requirement of employment as a trader stricken. *Id.* at 350.

482. Ostrow, *supra* note 102, at 102, 103 n.93.

483. Tabb, *Evolution*, *supra* note 480, at 351.

484. *In re* Klein, 42 U.S. (1 How.) 277 (1843).

485. *In re* Law Research Serv., Inc., No. 71-B-598 (S.D.N.Y. Dec. 9, 1971); *see* Asa S. Herzog, *The Case for Jury Trials on the Issue of Dischargeability*, 46 AM. BANKR. L.J. 235 (1972). This result was strongly criticized. *See* Merrill v. Walter E. Heller & Co. of Ala. (*In re* Merrill), 594 F.2d 1064, 1068 n.5 (5th Cir. 1979), *overruled on other grounds*, Garner v. Lehrer (*In re* Garner), 56 F.3d 677, 679 n.2 (5th Cir. 1995); Countryman, *supra* note 480.

486. *E.g.*, Varney v. Varney (*In re* Varney), No. 94-2045, 1996 WL 138684, at *2 (4th Cir. Mar. 28, 1996) (per curiam); *In re* Maurice, 21 F.3d 767, 773 (7th Cir. 1994) (en banc); Wachovia Bank & Trust Co. v. Banister (*In re* Banister), 737 F.2d 225, 226 n.2 (2d Cir. 1984); *In re* Merrill, 594 F.2d at 1068, *overruled on other grounds*, *In re Garner*, 56 F.3d at 679 n.2; *In re* Swope, 466 F.2d 936, 938 (7th Cir. 1972), *cert. denied*, 409 U.S. 1114 (1973); Schieber v. Hooper (*In re* Hooper), 112 B.R. 1009, 1012 (B.A.P. 9th Cir. 1990).

487. Countryman, *supra* note 480, at 36–39.

488. *See* Deitz v. Ford (*In re* Deitz), 469 B.R. 11, 20 (B.A.P. 9th Cir. 2012); Dragisic v. Boricich (*In re* Boricich), 464 B.R. 335, 337 (Bankr. N.D. Ill. 2011); Farooqi v. Carroll (*In re*

law, came to the same conclusion, and overruled the debtor's objection predicated upon *Stern*.[489] Relying on numerous post-*Stern* decisions, the court found that the discharge is "a fundamental part of the bankruptcy process."[490] In his concurrence, Judge Markell highlighted that the singular basis of discharge as a statutory right, without a common-law or non-statutory analog, places it squarely "within Congress's power to determine how to dispense and bestow the benefit."[491] The Constitutional Power of bankruptcy courts over dischargeability seems uncontroversial.

B. *Liquidation*

The action to liquidate a nondischargeable debt is an action "against the debtor, not against the estate."[492] Nonetheless, all the circuit courts that have confronted the issue allow bankruptcy judges to liquidate nondischargeable debts.[493] However, the circuit courts analyzed whether the liquidation of the nondischargeable claim was a core proceeding, not whether it passed either prong of the *Stern* test. Better precedent for the *Stern* analysis can be found in cases employing Seventh Amendment precedent to liquidation of nondischargeable debts. There, the scoreboard is more equal. The reasons for allowing blanket bankruptcy court adjudication—including waiver, administrative efficiency, and even the reinstatement of the summary/plenary dichotomy—are unpersuasive. Although the claims allowance process may necessarily determine some liquidations, in many cases claims are not filed because the case is a no-asset chapter 7. In most cases where the claims allowance process does not necessarily resolve all issues presented by the liquidation of the nondischargeable debt, liquidation of a nondischargeable debt should be treated like a state-law-based action against the debtor, not an action that is necessarily resolved by the claims allowance process or an action that stems from the bankruptcy itself. However, when all factual and legal issues presented by the liquidation would be adjudicated as part of deciding nondis-

Carroll), 464 B.R. 293, 312 (Bankr. N.D. Tex. 2011); Sanders v. Muhs (*In re* Muhs), No. 09-10564, 2011 WL 3421546, at *2 (Bankr. S.D. Tex. Aug. 2, 2011).

489. *In re Deitz*, 469 B.R. at 20.

490. *Id.* (quoting *In re Carroll*, 464 B.R. at 312).

491. *Id.* at 26 (Markell, J., concurring).

492. *Id.* at 27 (Markell, J., concurring).

493. Islamov v. Ungar (*In re* Ungar), 633 F.3d 675, 679 (8th Cir. 2011); Johnson v. Riebesell (*In re* Riebesell), 586 F.3d 782, 793–94 (10th Cir. 2009); Morrison v. W. Builders of Amarillo, Inc. (*In re* Morrison), 555 F.3d 473, 478 n.3 (5th Cir. 2009); Cowen v. Kennedy (*In re* Kennedy), 108 F.3d 1015, 1017–18 (9th Cir. 1997); Longo v. McLaren (*In re* McLaren), 3 F.3d 958, 965–66 (6th Cir. 1993).

chargeability, the dischargeability allowance process should allow bankruptcy courts' Constitutional Power to encompass the liquidation.

1. Core v. Related

Prior to *Stern*, the questions surrounding liquidation of nondischargeable debts centered upon whether bankruptcy courts possessed subject matter jurisdiction over the action.[494] Because *Stern* held that subject matter jurisdiction was not sufficient to overcome the obstacle of required Article III adjudication, these cases are not direct precedent for the *Stern* analysis. Yet, many bankruptcy courts have determined that they are bound by the applicable circuit courts' determination that liquidating a nondischargeable debt is a core proceeding for the purposes of the *Stern* analysis.[495] Even though the analysis of core jurisdiction is not binding, that does not mean that no relationship between Article III adjudication and subject matter jurisdiction exists. In his concurrence in *In re Dietz*, Judge Markell expressed skepticism that a bankruptcy court's Constitutional Power extended to the common-law claim for liquidation because the grant of statutory jurisdiction is very tenuous.[496] The liquidation of the debtor's nondischargeable debts "exist[s] independent of the bankruptcy process" and therefore does not "arise in" or "arise under" the Code.[497] At best, subject matter jurisdiction is proper because the actions are "related to bankruptcy"[498] and liquidation falls within the powers of § 105(a).[499] Such a questionable grant of subject matter jurisdiction is difficult to square with the power stemming from the bankruptcy itself in satisfaction of *Stern's* first prong.[500]

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494. *See, e.g.*, Gradco Corp. v. Blankenship (*In re* Blankenship), 408 B.R. 854, 864 & n.6 (Bankr. N.D. Ala. 2009) (listing cases).

495. *See In re Deitz*, 469 B.R. at 22–24; *In re* Carroll, 464 B.R. at 312–13; Christian v. Kim (*In re* Kim), No. 10-54472-C, 2011 WL 2708985, at *2 n.5 (Bankr. W.D. Tex. July 11, 2011); *cf.* Neves v. Markwood Invs. Ltd. (*In re* Neves), No. 11-24505-CIV, 2012 WL 1831717, at *3 (S.D. Fla. May 17, 2012) (finding other circuit courts persuasive).

496. Chief Judge Jones of the Fifth Circuit admitted that the analysis employed has "relied principally on tradition and pragmatism." *In re Morrison*, 555 F.3d at 479.

497. *In re Deitz*, 469 B.R. at 27 (Markell, J., concurring).

498. *Id.* (citing Brubaker, *Federal Bankruptcy Jurisdiction*, *supra* note 42, at 914–15).

499. *See* Sasson v. Sokoloff (*In re* Sasson), 424 F.3d 864, 868 (9th Cir. 2005) (noting that the links between dischargeability and liquidation make reliance by § 105(a) reasonable) (explaining that it is nonjurisdictional, however, greater analysis is required); *In re Deitz*, 469 B.R. at 27 (Markell, J., concurring).

500. *In re Deitz*, 469 B.R. at 29 (Markell, J., concurring).

2. Jury Trial

Prior to the Discharge Amendments,[501] bankruptcy courts did not determine the effect of discharge on specific claims.[502] The concept of dischargeability was unknown prior to 1970.[503] Before the Discharge Amendments, the process of determining the scope of discharge started when a bankruptcy court entered a debtor's discharge. A creditor seeking to evade the discharge could then sue the debtor on a specific claim in state court, and the debtor could raise the discharge as an affirmative defense.[504] The state court proceedings would then adjudicate the effect of the discharge by adjudicating the merits of the creditor's claim and, if necessary, liquidate the debt.[505] If requested, a jury trial would be used in the state court proceedings.[506]

The Discharge Amendments potentially allowed a bankruptcy referee to summarily liquidate a debt following a finding of nondischargeability.[507] If a referee determined that the claim was not dischargeable, pursuant to § 17(c) of the 1898 Act, he was required to "determine the remaining issues, render judgment, and make all orders necessary for the enforcement thereof."[508] However, the right to a jury trial was expressly retained: "Nothing in this subdivision c shall be deemed to affect the right of any party upon timely demand, to a trial by jury where such right exists."[509] Although uncertainty remained,[510] some courts applied this protection to the liquidation of nondischargeable claims under § 17(c)(3).[511] Hence, the Fifth Circuit and the Seventh Circuit held that, even though a debtor did not have a right to a jury trial on the issue of dischargeability, the debtor could be

501. Act of Oct. 19, 1970, Pub. L. No. 91-467, § 7(c), 84 Stat. 990, 992.

502. Merrill v. Walter E. Heller & Co. of Ala. (*In re* Merrill), 594 F.2d 1064, 1068 (5th Cir. 1979), *overruled on other grounds*, Garner v. Lehrer (*In re* Garner), 56 F.3d 677, 679 n.2 (5th Cir. 1995).

503. *In re* Copeland, 412 F. Supp. 949, 951, 953 (D. Del. 1976) (noting that a somewhat similar practice of a "split discharge" was used prior to 1970 amendments); Countryman, *supra* note 480, at 9.

504. *In re Merrill*, 594 F.2d at 1068, *overruled on other grounds*, *In re Garner*, 56 F.3d at 679 n.2.

505. *Id.*; *In re Copeland*, 412 F. Supp. at 952 n.5.

506. *In re Merrill*, 594 F.2d at 1068, *overruled on other grounds*, *In re Garner*, 56 F.3d at 679 n.2.

507. Bankruptcy Act of 1898, ch. 541, § 38(4), 30 Stat. 544, 555 (repealed in 1978 after significant amendments).

508. Act of Oct. 19, 1970, Pub. L. No. 91-467, § 7(c), 84 Stat. 990, 992.

509. *Id.*

510. *See In re Copeland*, 412 F. Supp. at 951, 953.

511. *In re Merrill*, 594 F.2d at 1068, *overruled on other grounds*, *In re Garner*, 56 F.3d at 679 n.2; Countryman, *supra* note 480, at 35. Professor Countryman was one of the principal drafters of the 1970 amendments. *In re* Swope, 466 F.2d 936, 938 (7th Cir. 1972).

entitled to a jury trial for liquidation of the nondischargeable debt.[512] When the Discharge Amendments were enacted, it was unsettled whether referees could try jury cases.[513] Some courts followed the policy of the Judicial Conference of the United States that "referees in bankruptcy should not try jury cases," including liquidation of nondischargeable debts.[514] Especially given the lack of evidence about concern for separation of powers problems, the power of a referee to summarily liquidate a nondischargeable debt is questionable. According to the legislative history, the Code did not incorporate § 17 because it was "unnecessary, in view of the comprehensive grant of jurisdiction."[515] Even if this legislative history evidences Congress's desire to allow for bankruptcy court liquidation of nondischargeable debts,[516] *Stern* teaches that such desire does surmount Article III infirmities.

Following the enactment of the Code, courts have split over the availability of a jury trial for a proceeding to liquidate a nondischargeable debt.[517] Courts finding that the right to a jury trial cannot attach to the liquidation of nondischargeable debts have relied upon two grounds: administrative efficiency and waiver.[518] Neither is convincing.

The administrative efficiency argument is typified by the Seventh Circuit's dictum in *N.I.S. Corp. v. Hallahan* (*In re Hallahan*).[519] *In re Hallahan* found "it preferable to allow bankruptcy courts ruling on the dischargeability of a debt to adjudicate the issues of liability and damages also."[520] *In re Hallahan's* preference stemmed from the "cumbersome process" of empanelling a jury in bankruptcy court, sending

512. *In re Merrill*, 594 F.2d at 1068, *overruled on other grounds*, *In re Garner*, 56 F.3d at 679 n.2; *In re Swope*, 466 F.2d at 938, *cert. denied*, 409 U.S. 1114 (1973).

513. Countryman, *supra* note 480, at 42–43.

514. *In re* Sneider, 59 F.R.D. 391, 394 (S.D.N.Y. 1973) (noting that the paucity of decisions on this issue makes it too uncertain to suggest a majority or minority view).

515. S. REP. No. 95-989, at 77 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5863; H.R. REP. No. 95-595, at 363 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6319.

516. *But see* First Omni Bank, N.A. v. Thrall (*In re* Thrall), 196 B.R. 959, 965 (Bankr. D. Colo. 1996) (criticizing the view that the legislative history supports bankruptcy court jurisdiction extending to liquidation of nondischargeable debts based upon the legislative history).

517. *Compare* Boudle v. CMI Network, Inc., No. 07-CV-2820(CPS)(SMG), 2007 WL 3306962, at *4 (E.D.N.Y. Nov. 6, 2007), *and* M. Sobel, Inc. v. Weinstein (*In re* Weinstein), 237 B.R. 567, 575 (Bankr. E.D.N.Y. 1999), *with* M C Contractors, Inc. v. Fink (*In re* Fink), 294 B.R. 657, 660 (W.D.N.C. 2003).

518. *Cf.* Johnson v. Riebesell (*In re* Riebesell), 586 F.3d 782, 793–94 (10th Cir. 2009).

519. 936 F.2d 1496, 1508 (7th Cir. 1991); *see In re Fink*, 294 B.R. at 660.

520. *In re Hallahan*, 936 F.2d at 1508. *But cf.* Porges v. Gruntal & Co. (*In re* Porges), 44 F.3d 159, 165 & n.7 (2d Cir. 1995).

the proceeding to the district court for empanelling, or referring the matter to state court.[521]

In *In re Weinstein*, the court persuasively analyzed why bifurcation of a nondischargeability proceeding between a nonjury dischargeability adjudication and a jury trial on liquidation was necessary, even though the process would be inefficient.[522] Although the court in *In re Weinstein* admitted the swiftness of liquidating the nondischargeable debt without a jury was tempting, it would "profoundly slight[ ] the constitutional dimension of the Seventh Amendment right to a jury trial."[523] Like the comments at the end of the majority opinion in *Stern*,[524] the court stressed that constitutional rights should not be overridden in the name of efficiency.[525]

In its alternative holding, *In re Hallahan* suggested that the filing of a petition waives a debtor's right to a jury trial on all issues.[526] The court reasoned that a debtor should not be able to seek sanctuary in bankruptcy and then retain the right to a jury trial while creditors, who necessarily file proofs of claim, lose their rights.[527] Hence, a debtor who voluntarily files a bankruptcy petition waives the right to a jury trial for all proceedings in the bankruptcy.[528] In *Longo v. McLaren* (*In re McLaren*), the Sixth Circuit subsequently adopted this rationale and found that a debtor's filing of a bankruptcy petition "stripped him of any right to a jury trial he might otherwise have claimed" for a nondischargeability proceeding.[529] Many courts have criticized *In re Hallahan's* waiver analysis.[530] The Fifth Circuit commented that the only effect of filing a petition "is to pass ownership

521. *In re Hallahan*, 936 F.2d at 1508.

522. 237 B.R. at 575.

523. *Id.* at 573. *But cf.* Germain v. Conn. Nat'l Bank, 988 F.2d 1323, 1330 (2d Cir. 1993) ("We will not presume that the same creditor or debtor has knowingly and willingly surrendered its constitutional right to a jury trial for the resolution of disputes that are only incidentally related to the bankruptcy process.").

524. *See* Stern v. Marshall, 131 S. Ct. 2594, 2619–20 (2011).

525. *In re Weinstein*, 237 B.R. at 573–74.

526. 936 F.2d at 1505.

527. *Id.*

528. *Id.* at 1505 n.10.

529. Longo v. McLaren (*In re* McLaren), 3 F.3d 958, 961 (6th Cir. 1993).

530. *E.g.*, Southmark Corp. v. Coopers & Lybrand (*In re* Southmark Corp.), 163 F.3d 925, 935 n.16 (5th Cir. 1999) ("[D]ebtor does not waive the right to a jury trial by filing a voluntary bankruptcy case."); Billing v. Ravin, Greenberg & Zackin, P.A., 22 F.3d 1242, 1251–52 (3d Cir. 1994); *id.* at 1257–58 (Sloviter, C.J., dissenting); Germain v. Conn. Nat'l Bank, 988 F.2d 1323, 1330 (2d Cir. 1993); *In re* Jensen, 946 F.2d 369, 373 (5th Cir. 1991); OHC Liquidation Trust v. Credit Suisse (*In re* Oakwood Homes Corp.), 378 B.R. 59, 70 (Bankr. D. Del. 2007); Quarles v. Wells Fargo Home Mortg., Inc. (*In re* Quarles), 294 B.R. 729, 730 (Bankr. E.D. Ark. 2003); WSC, Inc. v. Home Depot, Inc. (*In re* WSC, Inc.), 286 B.R. 321, 332 (Bankr. M.D. Tenn. 2002).

and control of the claims to the estate."[531] It is not sufficient to eliminate the jury trial right.[532] Moreover, the filing of the petition does not automatically start the claims allowance process,[533] much less necessarily resolve all issues presented by an action.[534] Lastly, *In re Hallahan* left unanswered the obvious issue of whether an involuntary debtor also waived all jury trial rights.[535] Taking *Hallahan's* reasoning one step further, one could find that creditors who join in an involuntary petition waive their jury trial rights. As one court explained in finding that a creditor who filed an involuntary petition had not waived the right to an Article III adjudication:

> While the filing of a proof of claim may invoke the claims resolution process in bankruptcy, the filing of an involuntary petition does not do so. In no way can a petitioner be charged with anticipating all outcomes of the filing, such that his act may be interpreted as the knowing relinquishment of rights that might arise at a stage much later in the involuntary bankruptcy case.[536]

Similarly, a debtor does not waive all his rights to a jury trial or Article III adjudication by simply filing a voluntary petition.[537]

3. Claims Allowance Process

Stern counseled that a bankruptcy court's Constitutional Power extends only to common-law actions which must be necessarily resolved as part of the claims allowance process. In the context of nondischargeability, the bankruptcy court's ruling on the proof of claim would have to necessarily determine all legal and factual issues arising from the liquidation of the nondischargeable debt. The claims allowance process has only limited application. In some situations, the overlap will not be complete while in no-asset chapter 7 cases, no estate will be created and the claims allowance process will be inapplicable.

Although it would seem that adjudicating a creditor's proof of claim and liquidating a nondischargeable debt based upon that claim would

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531. *In re Jensen*, 946 F.2d at 373.

532. *See In re Oakwood Homes Corp.*, 378 B.R. at 70 ("[L]egal claims are not magically converted into equitable issues by their presentation to a court of equity." (quoting Ross v. Bernhard, 396 U.S. 531, 538 (1970)) (internal quotation marks omitted)).

533. For instance, no estate is created when a no-asset chapter 7 is filed and a creditor follows the trustee's instruction to not file claims.

534. *Billing*, 22 F.3d at 1251–52.

535. N.I.S. Corp. v. Hallahan (*In re* Hallahan), 936 F.2d 1496, 1505 n.11 (7th Cir. 1991).

536. Tabor v. Kelly (*In re* Davis), No. 05-15794-GWE, 2011 WL 5429095, at *13 (Bankr. W.D. Tenn. Oct. 5, 2011).

537. *In re* Southmark, 163 F.3d 925, 935 n.16 (5th Cir. 1999) ("[A] debtor does not waive the right to a jury trial by filing a voluntary bankruptcy case.").

always satisfy the second prong of *Stern*, that is not the case. As explained by *First Omni Bank, N.A. v. Thrall* (*In re Thrall*), the claims allowance process and dischargeability are governed by separate provisions of the Code and the Federal Rules of Bankruptcy Procedure.[538] Once an objection to a claim is filed, a claim will not be allowed if the debtor proves it is unenforceable pursuant to "any agreement or applicable law."[539] In contrast, the liquidation of a nondischargeable debt determines what portion of a debt is not discharged.[540] If a creditor seeks a nondischargeability judgment on only a portion of its proof of claim, the factual issues determined in the claims allowance process will differ from those necessary to liquidate the nondischargeable debt.[541] Another example of the differences between the claims allowance process and liquidation of a nondischargeable debt arises when a party seeks post-petition interest accruing on the nondischargeable debt.[542] Section 502(b)(2) allows objections to such interest for creditors who are not oversecured.[543] In contrast, the interest could be part of liquidated nondischargeable debt. Thus, the proceeding to determine whether the post-petition interest is allowed as part of the claims allowance process requires different factual and legal analysis than determining whether the post-petition interest is an enforceable debt outside of bankruptcy: the analysis required for liquidating the nondischargeable debt.[544] The complete overlap required by *Stern* will not exist. Only if the debt represented in the proof of claim is the same as debt in the nondischargeability proceeding will resolving the proof of claim also resolve all factual and legal issues presented by the liquidation of the nondischargeable debt.[545]

Following *Stern*, the Eighth Circuit found that a complaint seeking liquidation of a nondischargeable debt can be necessarily resolved as

538. 196 B.R. 959, 966 (Bankr. D. Colo. 1996).

539. 11 U.S.C.A. § 502(b)(1) (West 2012).

540. This was not true under the 1898 Act. Under the 1898 Act, both the allowance and exceptions to discharge were limited by whether a debt was provable. *In re Thrall*, 196 B.R. at 965. The court would consider whether a debt was enforceable outside of bankruptcy and whether it was excepted from discharge in the same proceeding. *Id.* Thus, "creditors [used] the dischargeability proceeding for 'one stop shopping.'" *Id.*

541. *See id.* at 967.

542. Deitz v. Ford (*In re* Deitz), 469 B.R. 11, 29 (B.A.P. 9th Cir. 2012) (Markell, J., concurring).

543. § 502(b)(2).

544. *In re Deitz*, 469 B.R. at 29. The other limitations codified in § 502(b) create analogous problems. *Id.*

545. In the case of § 523(a)(2)(A), the Supreme Court's broad definition of debts obtained by fraud, including attorney fees, treble damages and costs, makes it more likely that the proof of claim debt and the nondischargeable debt will possess identical factual and legal issues. Cohen v. de la Cruz, 523 U.S. 213, 223 (1998).

part of the claims allowance process. In *Pearson Education, Inc. v. Almgren*, the court was confronted with whether a creditor who filed a proof of claim and a nondischargeability complaint against the debtor for willful copyright infringement retained the right to a jury trial for the damages portion of the nondischargeability complaint.[546] The court found that the creditor's proof of claim vitiated the creditor's right to a jury trial for liquidating the nondischargeable debt. Relying on *Stern*, the court found that resolving the creditor's proof of claim also liquidated the nondischargeable damages.[547]

The claims allowance process will not apply to every nondischargeability proceeding. The filing of the nondischargeability complaint could be deemed an informal proof of claim that would invoke the claims allowance process.[548] However, in a no-asset chapter 7 case when no bankruptcy estate is created,[549] a nondischargeability complaint does not invoke the claims allowance process.[550]

4. Stems from the Bankruptcy Itself

Looking beyond the claims allowance process, a number of post-*Stern* courts have held that the liquidation of a nondischargeable claim stems from the bankruptcy itself. *Farooqi v. Carroll* (*In re Carroll*) held that liquidation of a nondischargeable debt fit within the public rights exception because, in the words of *Thomas*, it is "closely integrated" with the Code.[551] Other courts have held that adjudication of the underlying action "becomes part and parcel of the dischargeability determination" and therefore stems from the bankruptcy itself.[552]

A number of potent arguments have been lodged against the liquidation of nondischargeable debts stemming from the bankruptcy itself. The action on the underlying debt is analogous to *Marathon's* and *Stern's* state-law-based actions because it is "a state law action independent of the federal bankruptcy law."[553] It "is totally unrelated

546. 685 F.3d 691, 693, 695 (8th Cir. 2012).

547. *Id.*

548. *In re Deitz*, 469 B.R. at 28 n.3 (Markell, J., concurring).

549. *See* FED. R. BANKR. P. 2002(e) (allowing a trustee to notify creditors to not file claims if it appears that there will be no dividends paid).

550. *In re Deitz*, 469 B.R. at 28 n.3; M. Sobel, Inc. v. Weinstein (*In re* Weinstein), 237 B.R. 567, 575 (Bankr. E.D.N.Y. 1999). *Contra* Heater v. Household Realty Corp. (*In re* Heater), 261 B.R. 145, 150 (Bankr. W.D. Pa. 2001).

551. Farooqi v. Carroll (*In re* Carroll), 464 B.R. 293, 312 (Bankr. N.D. Tex. 2011).

552. *See* Stanbrough v. Valle (*In re* Valle), 469 B.R. 35, 43 (Bankr. D. Idaho 2012). Although *Valle* is a jury trial case, it uses the phrase "integral to restructuring the debtor–creditor relationship," which this Article equates with "stems from the bankruptcy itself." *See supra* note 118.

553. Stern v. Marshall, 131 S. Ct. 2594, 2611 (2011); *see In re Weinstein*, 237 B.R. at 576; Ralph Brubaker, *Bankruptcy Court Jurisdiction to Enter a Money Judgment on a Nondischargeable*

to the administration of the debtor's bankruptcy estate and liquidation of the assets of that estate."[554] Its "only significance . . . is that the judgment creditor may be able to execute against the nonexempt portion of any future earnings or acquisitions of the debtor."[555] With such limited ties, it is doubtful whether liquidation of a nondischargeable debt always stems from the bankruptcy itself.[556] *Johnson v. Weihert* (*In re Weihert*) recently held that a bankruptcy court's Constitutional Power did not extend to liquidating a nondischargeable debt.[557] Echoing concerns raised by cases analyzing the Seventh Amendment, liquidation of the nondischargeable debt did not stem from the bankruptcy itself because "a non-dischargeable debt is not necessary to administer the bankruptcy estate, and dischargeability can be determined independent of liquidation."[558]

The most obvious argument for bankruptcy courts' constitutional adjudication of the liquidation of a nondischargeable debt is the reinstatement of the summary/plenary dichotomy.[559] Hence, if *Marathon* and *Stern* constitutionalized the summary/plenary divide, a bankruptcy court could potentially liquidate a nondischargeable debt based upon the practices employed under the Discharge Amendments.[560] However, unlike the claims allowance process in *Katchen*, the constitutionality of summary liquidation of a nondischargeable debt was not tested in the crucible of the Supreme Court prior to the enactment of the Code. Especially considering the Discharge Amendments' enactment barely predated the enactment of the Code and their limits were not well settled, it would be presumptuous that the pre-Code enactment itself is sufficient.[561] Moreover, it is unclear what part, if any,

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Debt: Exposing Pacor's *Deficiencies and the True Supplemental Nature of Third-Party "Related to" Bankruptcy Jurisdiction*, 29 No. 4 BANKR. L. LETTER 1, 10 (2009) [hereinafter Brubaker, *Bankruptcy Court Jurisdiction*].

554. Brubaker, *Bankruptcy Court Jurisdiction*, *supra* note 553, at 10.

555. *In re Weinstein*, 237 B.R. at 575.

556. Although not addressed here because it would require an article all by itself, one plausible way to find that the liquidation stems from the bankruptcy itself would be an incorporation of *Central Virginia Community College v. Katz*, 546 U.S. 356 (2006), and *Tennessee Student Assistance Corp. v. Hood*, 541 U.S. 440, 447 (2004). *See* West v. Freedom Med., Inc. (*In re* Apex Long Term Acute Care–Katy, L.P.), 465 B.R. 452, 462–63 (Bankr. S.D. Tex. 2011); Sanders v. Muhs (*In re* Muhs), No. 09-10564, 2011 WL 3421546, at *1–2 (Bankr. S.D. Tex. 2011).

557. Johnson v. Weihert (*In re* Weihert), No. 12-10893, 2013 WL 485878, at *4 (Bankr. W.D. Wis. Feb. 6, 2013).

558. *Id.*

559. Brubaker, *Bankruptcy Court Jurisdiction*, *supra* note 553, at 10.

560. *Id.*; Brubaker, *Statutory and Constitutional Theory*, *supra* note 8, at 173.

561. *Cf. In re Apex Long Term Acute Care–Katy, L.P.*, 465 B.R. at 463 ("The historical understanding of the plenary/summary distinction informs, but does not dictate, the Court's analysis of whether matters are integrally related to the claims adjudication process.").

the separation of powers issue played in the enactment of the Discharge Amendments.

5. Dischargeability Allowance Process

The dischargeability allowance process is comparable to the claims allowance process as it would allow the resolution of state-law-based actions to liquidate nondischargeable debts when all factual and legal issues will be determined as part of adjudicating a debt's nondischargeability.[562] It applies the res judicata concerns of *Katchen* to constitutionally allow the liquidation of a nondischargeable debt within the framework of *Stern*. *Stern* discussed how the summary adjudication of the claim in *Katchen*, together with issue and claim preclusion, made the otherwise necessary plenary suit to surrender a preference superfluous.[563] Because the issues would be resolved in ruling on the objection to the creditor's poof of claim, "nothing remains for adjudication in a plenary suit" and such a suit "would be a meaningless gesture."[564] This result is a consequence of the claims allowance process, the price required of creditors who seek distributions from the debtor's estate.[565] The Sixth Circuit recently applied similar logic to affirm a bankruptcy court's Constitutional Power to adjudicate the liabilities owed by a transferee of a fraudulent transfer who had a partial defense of good faith.[566] In the process of ruling on the creditor's proof of claim and the trustee's accompanying fraudulent transfer action, the bankruptcy court found that the assets transferred to the debtor by the creditor were worth $6.9 million.[567] The bankruptcy court also found the fraudulent transfer from the debtor to the creditor totaled $13 million.[568] The Court of Appeals found that the bankruptcy court could then constitutionally adjudicate the creditor's liability by subtracting the value conferred from the amount transferred by the debtor. The simple subtraction left after resolving the creditor's proof of claim and other issues necessarily resolved in the claims allowance process fit within *Katchen's* allowance for bank-

562. Sheets v. Carter (*In re* Carter), No. 11-53071-JDW, 2012 WL 3440431, at *3 (Bankr. M.D. Ga. Aug. 15, 2012).

563. Stern v. Marshall, 131 S. Ct. 2594, 2616 (2011) (citing Katchen v. Landy, 382 U.S. 323, 334 (1966)).

564. *Id.* (quoting *Katchen*, 382 U.S. at 334) (internal quotation marks omitted).

565. *Id.* (citing *Katchen*, 382 U.S. at 334).

566. Onkyo Eur. Elecs. GmbH v. Global Technovations Inc. (*In re* Global Technovations Inc.), No. 11-1582, 2012 WL 4017386, at *14 (6th Cir. Sept. 13, 2012).

567. *Id.* at *4.

568. *Id.*

ruptcy court determinations where "nothing remains for adjudication."[569]

The dischargeability allowance process is comparable. As noted by Judge Markell in *In re Deitz*, the facts adjudicated in the dischargeability proceeding in bankruptcy court often have a preclusive effect on the later court liquidating the debt.[570] In some cases, the later suit may be unnecessary, like the plenary suit in *Katchen*, because all factual and legal issues will have been decided in the nondischargeability suit. Analogous to the claims allowance process, the dischargeability allowance process is a consequence of a debtor seeking the protection of the bankruptcy court.[571] The reward of a fresh start with a full discharge is available only for the "honest but unfortunate debtor."[572]

However, the dischargeability allowance process should allow liquidation of a nondischargeable debt only when all factual and legal issues presented by the underlying state-law-based claim will be fully adjudicated as part of deciding nondischargeability.[573] *Sheets v. Carter* (*In re Carter*), is the first court to hint that it may apply the dischargeability allowance process to decide whether a bankruptcy court may constitutionally liquidate a nondischargeable debt.[574] It explained that a nondischargeable debt could be liquidated by a bankruptcy court only when all factual and legal issues were determined in

569. *Id.* at *14 (quoting *Stern*, 131 S. Ct. at 2616) (internal quotation marks omitted) (citing *Katchen*, 382 U.S. at 334).

570. Deitz v. Ford (*In re* Deitz), 469 B.R. 11, 28 (B.A.P. 9th Cir. 2012) (Markell, J., concurring) (citing *Katchen*, 382 U.S. at 334); *see also* Porges v. Gruntal & Co. (*In re* Porges), 44 F.3d 159, 165 (2d Cir. 1995); Stanbrough v. Valle (*In re* Valle), 469 B.R. 35, 43 (Bankr. D. Idaho 2012) ("In the case of an unliquidated debt, the bankruptcy court must necessarily determine liability and damages in order to establish the underlying debt. Adjudication of the underlying claim, which arises under nonbankruptcy law, becomes part and parcel of the dischargeability determination and thus integral to restructuring the debtor–creditor relationship.").

571. The consequences argument is weaker for the dischargeability allowance process even though at the time of the Code's enactment, the consequences of the filing of proof of claim were found in § 57(g), just like the consequences of filing the petition were found in § 38(4). These consequences were left out of the Code and have been subsequently added. Morrison v. W. Builders of Amarillo, Inc. (*In re* Morrison), 555 F.3d 473, 479 (5th Cir. 2009) ("The Bankruptcy Code did not specifically codify [the adjudication of liquidations] upon its enactment in 1978 . . . ."); *see* Ferriell, *supra* note 209, at 154.

572. Grogan v. Garner, 498 U.S. 279, 287 (1991).

573. Sheets v. Carter (*In re* Carter), No. 11-53071-JDW, 2012 WL 3440431, at *3 (Bankr. M.D. Ga. Aug. 15, 2012); *cf. In re Global Technovations Inc.*, 2012 WL 4017386, at *14 ("*Stern* cited with approval the Court's prior precedent holding that a bankruptcy court may award affirmative relief to a debtor after its creditor's proof of claim has been resolved and where nothing remains for adjudication." (quoting *Katchen*, 382 U.S. at 334) (internal quotation marks omitted)).

574. *In re Carter*, 2012 WL 3440431, at *3.

the process of deciding whether the debt was nondischargeable.[575] Other courts should follow its lead as the dischargeability allowance process tracks the teachings of *Stern* and *Katchen* to allow bankruptcy courts the Constitutional Power to liquidate a nondischargeable debt if all legal and factual issues will be determined in the process of deciding nondischargeability, even when the claims allowance process is not implicated.

VII. CONCLUSION

Although *Stern* potentially limits bankruptcy courts' Constitutional Power over many actions, without guidance on when its test should be applied, judges, practitioners, and commentators are left to hypothesize its limits. In *Granfinanciera,* the Supreme Court stated that it will provide answers for only the questions before it, instead of deciding every constitutional issue posed by the Reform Act and BAFJA.[576] Therefore, it appears that without congressional intervention, many years of litigation over the boundaries of the claims allowance process and what stems from the bankruptcy itself will ensue. In the meantime, the Seventh Amendment Case Line should be considered part of the Constitutional Adjudication Case Line, and courts should be wary of relying too heavily on the summary/plenary dichotomy. The relationship between *Stern* and discharge, specifically the liquidation of nondischargeable debt, should be further analyzed. The dischargeability allowance process profiled in this Article attempts to marry the concerns of *Stern* with the unique nature of discharge. Regardless, further detailed analysis of both prongs of the *Stern* test is necessary.

575. *Id.* The court further explained that the debtor's waiver of discharge would mean "the state law claims will no longer be decided in the process of determining dischargeability of those claims." *Id.*

576. Granfinanciera, S.A. v. Nordberg, 492 U.S. 33, 64 n.19 (1989).